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REAUTHORIZATION OF COMMUNITY AND URBAN DEVELOPMENT PROGRAMS

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BEFORE THE

SUBCOMMITTEE ON
HOUSING AND URBAN AFFAIRS

OF THE

COMMITTEE ON
BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

ONE HUNDRED FIRST CONGRESS

FIRST SESSION

ON

THE EFFORT TO REVITALIZE THE COUNTRY'S HOUSING AND COMMUNITY DEVELOPMENT POLICY BY FOCUSING ON COMMUNITY DEVELOPMENT BLOCK GRANT PROGRAMS

SEPTEMBER 8, 1989

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FRIDAY, SEPTEMBER 8, 1989

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON HOUSING AND URBAN AFFAIRS,
Washington, DC.

The subcommittee met at 10 a.m., in room SD-538 of the Dirksen Senate Office Building, Senator Alan Cranston (chairman of the subcommittee) presiding.

Present: Senators Cranston and Pressler.

OPENING STATEMENT OF SENATOR CRANSTON

Senator CRANSTON. The hearing will please come to order.

I thank all of you for your presence, particularly the members of the panel. We welcome your interest.

Today's hearing is an important part of the Housing Subcommittee's effort to revitalize the country's housing and community development policy. Our focus will be on community development block grants. We will consider the contributions that the program is making in following these committees across the country, and we will discuss ways to approve the CD block grant program so that it can be an even more effective tool for local communities in the future.

For 15 years CD block grants have been a keystone of the partnership among Federal, State, and local governments. CD block grants have stimulated an amazing ferment of problem solving and innovation. They have enabled thousands of local communities to explore better ways to develop their economies, better ways to meet urgent needs for job training and day care and housing rehabilitation.

CD block grants have helped nurture the rich variety of new partnerships among Government, the private sector, and nonprofit organizations, partnerships that are working to make local communities better places to work and live.

Fifteen years is a very long time for a Federal program to be successful in serving local communities. Rigid federally defined programs usually run out of steam and into serious problems after a few years, but CD block grants are more important to local problem solving today than ever, I believe. CD block grants have demonstrated the wisdom of carrying out national housing and community development objectives by providing a flexible and predictable Federal support to States and local governments.

In recent years block grants have been under intense pressure. Determined fights for funding have had to be waged year after year. Still they were cut by well over 40 percent in real terms. The previous administration trumpeted its support for block grants primarily as a way to divert attention from their devastation of Federal support for local communities. The Reaganite strategy was to lower block grant funding and broaden eligible activities so that block grants would be vulnerable to attacks that the program is diffuse and unable to achieve important national objectives.

And the hostile pressure continues. The budget imbalance is still being used as a reason to weaken block grants and to reduce the managerial flexibility of States and local governments. Appropriations so far have been held to the $3 billion level, but it is done by diverting funds from low income housing preservation and section 312 rehabilitation loans.

Important tools for local development, such as Section 108 loan guarantees and the lump sum drawdown are threatened once again this year.

I believe strongly that community development block grants must be given a clear national purpose. They must be assured of adequate funding, and they must continue as a cornerstone of federal housing and development policy.

I also believe that community development block grants must provide the maximum feasible degree of local managerial flexibility. I am determined to press for these objectives as this subcommittee works for landmark legislation to thoroughly reform the Department of Housing and Urban Development and revitalize national housing and development policy.

I want to assure you that the effort to enact major housing legislation is very alive and very well. Many of you here this morning played a large role during the past two and a half years in shaping the Cranston-D'Amato National Affordable Housing Act. When Congress refines that legislation and finally enacts it into law, it will include a strengthened and reauthorized community development block grant program. Passage of that legislation is the top priority of this subcommittee.

We are now refining the bill in the light of hearing testimony, and we are refining the bill to protect against any repetition of the Reagan Administration scandals at HUD. I am confident that landmark legislation will be enacted by this Congress, but an uphill battle remains before us. We will need your all-out and active support.

We are very fortunate to have an excellent group of witnesses this morning. Each of you have demonstrated skill and determination in using block grants to improve your communities' infrastructure, housing, and economy. I am grateful that each of you are here to help us examine the strengths and impediments in the CD block grant program.

I ask each of you to give us your best counsel so we can create the first-rate piece of housing and community development legislation that the country needs and that the people who need help in housing deserve.

We are holding this morning's hearings in the form of a roundtable discussion rather than a formal hearing. It is somewhat nontraditional for Senate hearings, but we are finding that this format allows our witnesses and members of the subcommittee and the committee itself to explore the major issues much more fully and usefully.

I encourage each of you to comment on areas where you disagree as well as where you agree. I think we learn more when we get some exchanges that indicate a different view, and then we can try to sort that out. So don't hesitate to challenge if you disagree with something that is said by anybody. We usually learn more from that vigorous airing of disagreements and differences in point of view than when you all agree on something.

So I look forward to our discussion and suggest that we now turn to the first issue, and that is in regard to the success of the CD block grant program.

Today I would like to start by going around the table and having each of our witnesses address two questions, and again don't wait for your turn if you feel like popping in with something, and we won't continue to go around the table. We will try to evolve from that as we get on, and we will just go back and forth with whoever feels like talking.

So two questions. What do you think are the two most valuable characteristics of the community block grant program? What are the two areas where the CD block grant program can be most usefully improved?

If you would speak as much as you can from your own firsthand experience, I would appreciate it.

Let's start with you, Mr. Swain. Thank you and all of you for being present.

JEFFREY SWAIN

Mr. SWAIN. Thank you very much, Senator.

I think clearly the two most important characteristics, valuable characteristics of the community development program from the local community's perspective is its local flexibility, which allows communities to respond to their respective needs, but within the framework of the national objectives that are laid out in the legislation.

This allows each community to address the needs, whether that be housing, human services, public improvements, and whatever mix seems to make best sense for that individual community, but at the same time of course responding to the national objectives of serving low and moderate income households primarily, as well as eliminating slums and blight.

I think the second major value of the program suggested in the flexibility, I suppose, is that it can be comprehensive. I think that is the lesson that can be learned from looking at the history of the legislation, how it came into being and the fact that it was a merger or consolidation of several categorical programs specifically for the purpose of being able to address the community's needs in a comprehensive way. We took urban renewal and we took the model cities program and several other programs and said to the local community through its local government, you can go ahead and plan for a broadly based set of initiatives which can respond to the human problems as well as physical problems of your neighborhoods in greatest need. So it is the comprehensiveness of it which is important.

And suggested there also is the significance of partnerships between the federal and local governments, the partnership with the communities, their individual residents, developing their own delivery systems and in many respects through community-based organizations and delivery of services a partnership also with the private sector.

I think, in summary, the most valuable characteristics of CDBG are the local flexibility to meet local needs, the comprehensiveness and the three-way partnerships between government and the private sector and its residents.

Senator **Cranston**. Thank you very, very much.

Monsignor Linder.

MONSIGNOR WILLIAM LINDER

Mr. **Linder**. I would like to say that in our experience in Newark, CD funds are used at times to leverage primary financing in economic development projects. New Community Corporation, the non-profit with which I am associated, has two such projects. One of the most valuable characteristics of CD funds is its flexibility.

I believe, however, that one of the characteristics of CD funds which needs improvement is further targeting for the needs of low income. The intent of the legislation is to serve low income people. Unfortunately, in my opinion the funds are frequently used for other purposes.

Further, there is a need to strengthen the role of non-profits so that non-profits can increase their participation. If our low income neighborhoods are to benefit, we need the participation of our non-profits.

I am part of the work of New Community Corporation, the most successful non-profit community development corporation in New Jersey. These types of organizations need to be expanded in number and strengthened because they are closest to the people.

Senator **Cranston**. Thank you very much.

There are three people here from California. Helen, thank you for coming.

HELEN SAUSE

Ms. **Sause**. Thank you, Senator. Thank you for conducting this hearing. This format provides a very good discussion opportunity.

Mr. Swain really set forth, I think, the development need for the CDBG in his statement outlining the value of local flexibility and the local decisionmaker's ability to use the program to address the different housing markets that we find across this country, and it is very important for each community to have a number of tools to renew blighted areas and to address their local needs in providing a holistic approach to neighborhood stabilization and revitalization.

So I can only echo that. Both in my community's experience and as I have traveled as a national president to other communities, we find great diversity in the small towns, the large towns, the coastal areas, and the center of the country.

But I would like to comment on some of the things that could be done to improve the programming.

Senator **CRANSTON**. Good. We will be glad to hear that.

Ms. SAUSE. The predictability of the funding is something that we have lived like the Perils of Pauline year after year, it is counter productive to wonder if it is going to be reauthorized and funds appropriated for the program each year.

Senator **CRANSTON**. If you could find a cure for that, I would be very grateful.

Ms. SAUSE. I think that we spend a tremendous amount of energy trying to keep the program alive.

Now, I would like to move to a phase where the program actually has a predictable authorization life span, as a suggestion three years, some predictable life span so we don't have to spend a tremendous amount of energy on keeping it available.

Another is the expanded uses for the program. There is a great temptation to use it, as other programs are terminated, to fill new and unexpected uses. So it is very important that the national objectives that have been set, be the ones that we adhere to, not interjecting new things like the use of CDBG to fund 911 and these kinds of things that erode the national objectives of this program.

I disagree slightly with Mr. Linder in the need to set aside or establish a particular kitty for the nonprofits. I think nonprofits are very valuable and, like Mr. Linder, in my city we work very directly with nonprofits to a large extent, but I would like the flexibility of the local decisionmakers making the decision on how those allocations are made and where the partnerships are valuable. The local decisionmakers are the best ones to establish that value rather than having a mandate that a certain amount of funds be set aside for a certain group.

In some states there are no nonprofits or only one or two, but I think the local decisionmakers have the wisdom to decide how those funds should be allocated, and the real objective is to stay within the national objectives for the program's use.

Senator CRANSTON. Thank you very much.

Mr. Middleton.

ROBERT K. MIDDLETON

Mr. MIDDLETON. I appreciate your calling this session and the opportunity to visit with you.

I guess, representing the states, probably the key most valuable characteristic of the program is its flexibility. It is very rare to see a domestic program that has the capacity to meet both urban and rural needs all out of one piece of legislation. That flexibility, it just seems to me, needs to be kept. It is critical. It is key.

Second, to the extent that there is targeting in the program, even if it is somewhat general, it forces a real discussion of priority setting at the local level, which especially in rural communities is very critical, an area where the block grant we think would be usefully improved. A number of communities and states are trying to utilize funds to create revolving loan funds, either for housing allocation or economic development activities, so that we don't spend the allocation and get one shot and then continue the federal level for more.

Treasury required us to spend program income prior to getting new allocation out, which means that we will not have the capacity to develop more of these funds available in the future years. To us that is critical because in Arkansas we are utilizing CDBG assistance to hook up with welfare reform programs. CDBG is very useful in terms of job generation, which is critical, education, and really health and welfare dependency are going to occur.

Senator **CRANSTON**. Thank you very much.

Mr. Finkle.

JEFFREY A. FINDLE

Mr. **FINKLE**. Thank you, Senator.

I think it is clear that what Mr. Swain at the beginning said as the most important aspect of the community development block grant program is the ability for local flexibility. Local governments can make the determinations in terms of what they want to use their dollars for. If they need to rehab housing on a large scale basis, they have that flexibility to do so. If the concern is that many people in the low income categories would be underserved in job creation and entrepreneurial opportunities, local governments can make that determination.

So I think the flexibility is clearly an issue which is the most valuable part of it, of the community development program.

Two aspects of the program that we think can be most usefully improved are to stop the reregulation of the program. We are finding a tightening and tightening of the regulations to the program, so much so that economic development, for example, is becoming harder and harder to do at the local level.

In a survey that was undertaken by the Department of Housing and Urban Development about two years ago, about one dollar out of eight dollars spent in community development block grant programs are for job creation programs. We are seeing a reduction of that to about one in ten dollars during the last period, the survey undertaken by the Department of Housing and Urban Development, and based on the complaints and concerns that we are hearing from our membership across the country, we expect that that is going to be significantly less during their next reporting period.

The second issue that is of concern is the issue of the Davis-Bacon wage requirements that occur when construction occurs through the community development block grant program, and we see that as effectively wasting approximately $200 to $300 million of the community development block grant program money on a yearly basis in trying to meet the requirements of Davis-Bacon.

But the important tool I think that the block grant program provides, in summation, is the local flexibility that that offers to local governments.

Senator **PRESSLER**. Mr. Finkle, I would just like to add a footnote there. I think Davis-Bacon is a real problem.

How do you recommend we alter that?

Mr. **Finkle**. I think where I think most of our members would like to see it go is raising the cap of applicability of the Davis-Bacon law so that it applies to much higher threshold projects than some of the local projects local governments are working on.

Senator **Pressler**. How much money could we save if we did that?

Mr. **Finkle**. I have not done that research, but we could certainly take a stab of making some type of guesstimate for you.

Senator **Pressler**. I would like you to do that and also submit it to me, if you could, for the record.

[The information referred to above follows:]

We estimate that raising the threshold of project size from $2,000 to $250,000 would save approximately $100 million per year. This is confirmed by experts in community development based on total CDBG expenditures in housing, public works and economic development.

Senator **Cranston**. Before we go to Ms. Melkonian, does anybody disagree with or want to amplify on anything that has been said?

Yes.

Mr. **Ray**. I guess my concern is not necessarily Davis-Bacon, but I think if there is in fact use of CDBG funds—and we talked about serving low and moderate income people, changing their quality of life—I don't think that those funds should be used without regulations. You know, there are situations where CDBG funds have been used and people are paid sub-minimum wage on labor wages. There are no standards, wage and hour standards, placed on that. There is no safety or health, occupational standards placed on that. There is no workmen's compensation.

So if we are truly talking about a program that is going to benefit people, then we are not going to talk about a program that would go back to something close to sweat shops and misuse of people.

Mr. **Swain**. Just one comment on the set-asides for community-based organizations. I would acknowledge, as I did, the significance of partnerships locally with community-based organizations, but would echo what Ms. Sause said about the set-asides. I think that would be really legislating implementation and delivery systems rather than national objectives, which would be most unfortunate.

I would say, though, that in 1986 the National Community Development Association did a survey and determined that at that point, at least, there were some 5,000 nonprofit organizations or community-based organizations around the country that were already participants in and very integral parts of the implementing of the community development program.

So I think the record is clear that as we sit here today that the nonprofit sector or the community-based organizations are in fact a very important portion of the implementation of the program, and we from the community development association perspective did not see the need for set-asides in the legislation. That would be much too limiting on the flexibility of the program and the nonprofits are already a major part of the program.

Senator **Cranston**. Any other comments on these particular points?

Mr. SCALLON. I would like to comment on the set-asides, also. The community development block grant idea is broader than one specific group. As you get to one specific group you miss the objectives. What happens if your neighborhood that you are serving has a commercial area and declaring all your nonprofits are only in housing? Does that mean the city cannot do anything for creating community economic development?

Most of us in the communities have done an awful lot. I have worked extensively in nonprofits. The city I am with actually sets aside money to support their administration CDBG, and they actually encourage them in terms of CDBG, instead of regulatory, which is divisive and takes the groups that support CDBG and gets them fighting among themselves, leading to the death of the program.

Why don't we look at rules that make it even more inclusive? For example, CDBG can only do new construction with nonprofit programs. Therefore, let us work with nonprofit corporations in new construction. It is a way that nonprofits are brought into the program.

I hope that your regulations are aimed at enhancing bringing nonprofits into the program rather than regulatory on top of groups that are all trying to provide the same kind of housing.

Ms. KELLY. Senator, may I make a comment on that point?

We represent 218 nonprofit companies around the country. I think I would agree with what has been said here, that a set-aside can very often become more restrictive than it can inclusive. I think our nonprofit network has made extraordinary use of community development block grants, but I would like to suggest and recommend that when a successful nonprofit in the community is a recipient of community development funds, there are things that can be done to facilitate the effective use of those funds by that organization. Reduce the amount of red tape that productive nonprofits are required to respond to—which is not to suggest that they shouldn't be monitored. I think if a nonprofit is working well in the community it is not a secret to anyone. I think we should try to find ways of helping successful nonprofits be more successful.

Mr. GRAMLICH. Senator, to continue the nonprofit theme, there are many, many nonprofits across the country that are very capable, who have demonstrated the capacity over the years, yet have difficulty getting CDBG money to do housing rehabilitation. And I think to have a set-aside would enable very capable organizations to have an easier time in securing this money.

We are not arguing that they should be guaranteed this money. They should be able to be competent and compete, but have easier access to money.

There is a lot of talk about this program having flexibility and decisionmaking by local people. Well, people in the neighborhoods, the people who control the nonprofits are very local. They should have an opportunity in that decisionmaking process to determine how the money is used to improve their community.

Senator CRANSTON. Anything else on this?

Larry, did you have any general opening remarks?

Senator PRESSLER. I have no statement for the record. Thank you.

Senator Pressler. Another subject is my co-sponsorship of the Sanford bill, in addition to the main bill, to protect rural and small town interests, which I am sure you are going to do anyway, Mr. Chairman. [Laughter.]

Senator Cranston. I think we might move on to the second question. I think you have all seen—and that relates to federal/local aspects of CDBG. I don't want to exclude further comments on the matter we have been discussing as we go around the table, but we might move on to the fact that one of the unique features of the CDBG is that it fosters a partnership between government at the federal and local levels.

Entitlement communities can plan ahead with some assurance that federal assistance will be available, and local communities can determine how best to use CDBG funds in their community. HUD religated to a generally oversight role. Some argue that more legislative direction should be given in the use of CDBG funds.

One proposal, for example, is that Congress should require that 25 percent of such funds be set aside for nonprofit organizations.

So the questions are—and there may be others, but the questions that I wanted to put to you are to what degree have nonprofit organizations been recipients of CDBG funds in recent years? What are the special benefits of using nonprofits? What would be the benefits and what might be the difficulties of the set-aside for nonprofits? And how might such a set-aside work?

May I go to you now, Ms. Melkonian, in that general area?

Ms. Melkonian. I would rather answer the other one. [Laughter.]

MARILYN MELKONIAN

Just to put my interests in context, we are working in a community here in Washington called Parkside, which is making use of CDBG funds. Nonprofits and for-profits are involved in it. Over $40 million of public and private investment is going into a neighborhood of about 7000 people, and all of the housing in that community is being renovated and additional new housing is going to be constructed.

As was pointed out, only nonprofits can use CDBG funds in construction of new housing. So obviously the program already has some openings for nonprofits to be primary participants.

It is my view that in the long run, given the trend of funding and legislation, in both housing and community development, that we are going to look more and more to the nonprofit community to be doing more of the things that need to be done in rehabilitating neighborhoods. It is worthwhile to consider how that force can be strengthened, not so much because it is nonprofit, because I think nonprofits have to make money doing these things, but because they have the dedication to take on these hard tasks, and over the long run public investment is returned by a permanent benefit. For example, in the housing field, in the prepayment area, the old 221(d)(3) and 236 projects; public investment did not result in permanent affordability. That would not have been the outcome if the ownership of those projects had been in nonprofit hands.

So I think that maximizing the long-term benefit of public investment is where nonprofits can be most useful.

Senator **Cranston**. Thank you very much.

Mr. Anderson.

PARKER ANDERSON

Mr. **Anderson**. Representing the city of Los Angeles——

Senator **Cranston**. Yes, I wanted to note another Californian.

Mr. **Anderson**. Actually, I would like to thank you for your opening statement. I found that very, very reassuring. The block grant program for our city is really the engine that drives most all of the programs which we target to those most especially in need. It provides the comprehensiveness and flexibility to enforce the kind of working relationships, both the federal government and the local entities, to really make things work effectively.

Despite all the disparate kinds of plans of other bills that come into place, the block grant really pulls everything together in the city.

Our community administers not only block grants but the community services administration funds. We have a whole range of issues with which we deal, and the block grant gives us that comprehensiveness and flexibility, which I guess brings me to the issue of the nonprofits.

I think the major issue here is philosophically what the block grant is all about. It seems to me that the thrust of the block grant is to meet the needs of low and moderate income people. That is their objective.

Then the question becomes are we confusing the means with an end? To me, what is the public sector, the for-profit private sector, the nonprofit private sector? Those are all means to an end. Those are all vehicles for delivering the types of services and activities that are necessary to improve the lives of those who are so desperately in need of those services.

I really am concerned that we presumptively start allocating and targeting funds to a type of delivery or emphasizing one of those means to that end.

In our particular program the last several years we have shifted our program funds about 40 percent to housing, with a tremendous emphasis in the single room occupancy problem, maintaining our affordable housing stock, not just the housing which we are losing as a result of the lapse of federal subsidies but as well as what we call skid row housing, where the single room hotels are being razed because of their age. We shifted to deal with the issue of AIDS. We have shifted to dealing with the issue of homelessness and facilities for the homeless individuals.

It is that flexibility, our ability to choose the most effective delivery mechanism to meet the needs of those individuals, which we feel is the hallmark of the block grant. That is why we do have a concern about any presumptive targeting to a means in this particular program.

I would also like to say that within the block grant, because of that flexibility, we have the opportunity to establish new types of things to facilitate nonprofits.

In the City of Los Angeles we do not have a well-entrenched history of nonprofit involvement in housing production. What we have established this year is what we call a nonprofit housing innovation fund for the first time to provide capacity building activities for nonprofits in housing, to provide financing and predevelopment funds, which is a real problem for nonprofits.

So because of the block grant's flexibility we are now able to move into a whole new area of emphasis, which is creating the capability at the local level for nonprofits being involved in housing in the City of Los Angeles, which they have traditionally not been. But to set aside a specific set of funds for nonprofits would really undermine that effort and that flexibility.

Senator **Cranston**. Thank you very much.

Yes?

Mr. **Middleton**. Senator, I would like to echo his comments. I think having a set-aside in effect creates a new national objective, which in effect is at least 25 percent of the funds must go to nonprofits, which is different from the objective we all support, which is for low and moderate income.

Further, the distribution to nonprofits is a very uneven distribution of nonprofit organizations around the country, depending on our definition of nonprofit organization. In rural areas we see a number of nonprofits who are involved in water delivery, solid waste delivery. There are so many nonprofits right now. The State of Arkansas has over 500 eligible direct applicants to the state for the nonprofit portion of the program. If you allow the nonprofits to apply without describing what in fact you are talking about, we could have several thousand applicants. It would become an administrative nightmare, and I think it would also dilute the accountability that government provides for the program.

Senator **Cranston**. Thank you very much.

Yes?

PREDDY RAY

Mr. **Ray**. I think it is important to follow up on one statement that has been said, that we limit this to entitlement programs, because the reality is as you get into your state and rural programs you get into a lot of different types of nonprofits which cannot be clearly defined.

We define nonprofits as neighborhood or community-based groups. It is interesting to note that people have a hesitancy of saying that set-asides should be made, but at the same time realize that you have a good, efficient, and effective delivery system, also realizing that the for-profit sector is moving out of the realm of CDBG for whatever reasons.

We think that there is a need for targeting and there is a need simply because the objective is to serve low and moderate income people, and nonprofit organizations have proved historically that they can do—specifically produce housing at a much cheaper rate.

In Richmond, VA, our organization, the Community Development Corp., can produce and rehab a unit at 30 percent lower than the private sector. It is a comparable unit. It is decent, it is affordable, and in some situations we go beyond decent and affordable.

I think that you have a group of organizations. Given the number of 5000, our group represents over 700, many of which produce housing, many of which are involved in commercial development, and we say that we have been eliminated in certain situations because CDBG has become, for lack of a better word—and in reality I am sitting next to a mayor—it has become a political slush fund. You can get 911's funded through CDBG. The planning department has been funded through other city funds, and they cut back the city funds. We get those positions from the CDBG.

We get a plethora of programs that come out of the minds of politicians that come into CDBG because it is a good and flexible program. We are just saying that if we truly want to hold to the national agenda of working with and providing for the benefit of low income people, here is an entity, nonprofit organizations, with a good track record, 5000 organizations across the country that can do it, that need a foot into the door and a foot into the door that would ensure not only that they can build their capacity, but that they can maintain it.

Senator **Cranston**. Mr. Gramlich, do you have a comment?

Mr. **Gramlich**. I would echo Preddy Ray's comment.

Senator **Cranston**. Mr. Scallon.

TONY SCALLON

Mr. **Scallon**. I will give you a little bit of my background. I am a former member of a nonprofit and formerly president of a neighborhood group and now a politician. So I have gone down. [Laughter.]

But when I was a neighborhood activist and before I was a politician the big issue was rental housing, and the nonprofit I was with created low income housing. We created a tremendous amount of low income housing through our nonprofits, except for one minor thing. There is a new crisis in the city, and people are leaving the city and they no longer need the rental units. We now need to do an FHA homesteading program using CDBG, since FHA won't work very easily with us, and we have a lot of boarded up buildings.

Now, suddenly—by the way, we make the 25 percent nonprofits. That won't affect us at all, but that is irrelevant. The point is we are ready. If we decide to go to the Board of Buildings and do homesteading, how do we do that if you have a rule saying you can't, you have to give so much money to one group, which may not be the appropriate response.

Then let me give you one other comment. In Minneapolis we have a sister city that is equally progressive and beautiful, called St. Paul, a wonderful city. It has very few nonprofits. It somehow does all the things for low and moderate income housing as well as we do. Using nonprofits, there isn't that nice, easy solution. That may be a solution in Richmond. What Barney Frank brought forward is a solution for Boston, but they often don't work in our Midwestern cities. What is good for my Midwestern city has no relationship to my brother-in-law, who lives in California. A home in my area is $70,000. He is paying out almost $300,000 for the same house. It is a different market.

So that is why a lot of us from the local government perspective and those of us who have been nonprofit members and who have been neighborhood activists say don't give up that flexibility in exchange for what you think will be a solution for another problem that you perceive.

Senator **CRANSTON**. How does it happen that there are so few nonprofits?

Mr. **SCALLON**. I would really have to ask St. Paul why. In Minneapolis we do have wonderful nonprofits, and they are the backbone of our CDBG program. St. Paul? I think it is because neighborhood groups have more power in St. Paul than in Minneapolis, not that they don't have it in Minneapolis, and the nonprofits have more authority in Minneapolis. I think the neighborhood groups have used the for-profits.

I want to mention the for-profits. We do use for-profits sometimes. In the last year they have been chiefly nonprofits. That does happen. It is not a nice, pure world.

But I would be interested to find out if the people in St. Paul have been able to bring in for-profits and direct the money in that direction. But in our area we have not had the investment by the for-profit community, and we need the nonprofits to bring in the resources.

Senator **CRANSTON**. Mr. Sarault.

BRIAN J. SARAULT

Mr. **SARAULT**. Thank you, Mr. Chairman. I happen to be the mayor, as Mr. Ray referred to earlier, from the East Coast, and I can certainly appreciate some of the concerns Mr. Ray brought up. I must say at the same time, from my experience in this area, flexibility has been—not to be redundant, but flexibility has been one of the essential elements. It has been the major factor in the success of the community development block grant program.

The question of a set-aside, even though in my community nonprofits are in fact major players, my concern in this area is I think flexibility is important to retain. I think Ms. Sause really brought out the fact that one of the major problems we have is the fact of the uncertainty of the funding in future years. This poses a very serious problem from any standpoint.

Obviously, I am an advocate, as the Conference of Mayors is, of at least maintaining the present level of funding and hopefully increasing the funding because only with programs such as this are we really able to allow and through the nonprofits to maintain and enhance the quality of life in our communities. So flexibility I believe is and has been due to the fact that every community has different needs, an essential factor in the success of this program.

Senator **CRANSTON**. Thank you.

Monsignor.

Mr. **LINDER**. Senator, I am also a member of the New Jersey Housing and Mortgage Finance Agency and as a member for 14 years it has taken me through two State Administrations in New Jersey.

Several years ago there was almost a consensus in our State that we needed to attract the for-profit building industry if we are going to solve our limited income housing needs. Frankly, this approach got us nowhere because the for-profit organizations would not go into areas of our communities where the State felt that housing was most needed.

The State is now concentrating more energy in assisting the non-profits, of which we have many in New Jersey. In fact, about half of the New Jersey Housing and Mortgage Finance Agency's multi-family portfolio originated from non-profits. There is need to strengthen these organizations since housing development has become more difficult and complex.

Why make a commitment to strengthen the non-profits? It is because the non-profits offer us the best chance of success in serving low income people. Frankly, it is our experience that we cannot afford the return which for-profits require when it comes to low income housing. So we are now turning to our non-profits who are responding.

I think we cannot forget our need for non-profit participation. Why should there be a non-profit set aside? Because non-profits obviously don't have the very sophisticated system of representing their interest as do the for-profits.

I would like to mention the experience of New Community, which now has partnerships with five major corporations in order to meet housing needs of low income people. Every one of these large corporations has a strong full time political action staff and non-profits don't have that assistance. So the only way to protect the participation of the non-profit, which is in the public interest, is to write it in the legislation.

Thank you, Senator.

Senator CRANSTON. Thank you.

Mr. Swain.

Mr. SWAIN. I would just observe, I don't think there is any disagreement in principle or in philosophy around this table about the significance and the importance of the nonprofits to the implementation of the community development program.

I think, as I alluded to earlier, our survey shows that 5,000 nonprofits were participants in the program in 1986, but what I take issue with is the notion just indicated by Mr. Linder of protection or that the means for program implementation should be laid out in the legislation. We certainly don't think that should be the case.

Just a couple of comments on the special benefits of nonprofit involvement in the CDBG. The nonprofits do provide very, very important functions in the delivery of the community development programs. The commitment of nonprofits, the commitment to their communities is unquestioned and is very important to us all. The grass roots nature of most nonprofits, many nonprofits, is very, very important.

In most cases their costs of delivering services—maybe that shouldn't be looked at as a positive because we know that many staff people in the nonprofits are very poorly paid, and that creates one of the problems, which is so much transition of staff in nonprofits, which at times creates problems in the stability of an agency—but nevertheless, their costs are lower for the most part in delivery of those services.

So there are very significant benefits to the involvement of nonprofits.

On the downside of the notion of set-asides, I think it would frustrate local planning, create obstacles to local planning efforts. It would create a sense that there is a right to getting money on the part of one sector of the community, which would frustrate the planning.

Some cities and communities around the country that we have had input from just simply do not have nonprofit vehicles at the current time. You could argue that this is one incentive for them to create nonprofits. But we don't see that as being prudent.

I think there is a bottom line from HUD's perspective on this. With a 25-percent non-profit set-aside, who then is accountable for the program? A mandated set-aside of 25 percent is going to create, I think, some problems for HUD. It is going to create problems for local government in giving the nonprofits a sense of right to the funding as well as then frustrating to some extent local governments' accountability for the program.

MARGARET KELLY

Ms. **Kelly**. Senator, another comment.

First, I would certainly urge anybody who doesn't have a nonprofit in their part of the country to talk to me after the session. I think there is an incredibly strong group of nonprofits across the country who are doing an extraordinary job, and we are getting requests on a daily basis from places like Bellows Falls, Vermont and small communities, medium size communities, larger communities.

Part of the problem with this discussion is simply that the pie is just too small. The complexity and the cost of doing business for nonprofits and the public sector has just become extraordinary and there are not enough funds to go around. The transactional cost to put together a deal often involves seven, eight, or nine funding sources, and it is a very complicated and expensive process to assemble these resources.

So I would just plead, in addition to this discussion, that we broaden it to talk about the feasibility of enlarging the pie.

EDWARD GRAMLICH

Mr. **Gramlich**. Senator, I would like to ask a question to Mr. Swain, if he fears that having nonprofits involved will make life more difficult for HUD.

Mr. **Swain**. I didn't say that.

Mr. **Gramlich**. The accountability was what you implied. I guess I would appreciate some clarification on that because I don't think that necessarily has to be the case. Nonprofits are accountable to their church funding sources, to their foundation funding sources, and to the local government to the extent that they are getting CDBG money. They are accountable to other jurisdictions, not just HUD.

Maybe there is an aspect of that that I am not clear about. I think that would be instructive for all of us.

Mr. **Swain**. I think there becomes a significant difference when currently nonprofits are funded based on a local planning process involving all sectors of the community. A local decision is made that the best delivery system involves contracting with a nonprofit. In our case most usually through a request for proposal for public services, housing outreach programs, whatever they may be.

My point was simply that if you insert a 25 percent criterion then nonprofits may well believe that they report directly to HUD or believe that no matter what they do the 25 percent is guaranteed. So you start to get problems on the margins potentially in terms of performance because they know they are guaranteed to get the 25 percent. That is the point that you start to lose accountability of the local oversight in the monitoring process.

Mr. **Gramlich**. There are often multiple nonprofits in any given neighborhood. So there could be competition instead of a guarantee of that money. A guarantee is not necessarily there, I don't believe, and I trust that HUD would be as diligent in its monitoring of local and neighborhood organizations as it would be of other entities receiving federal monies.

Mr. **Scallon**. Hold on. That isn't what HUD's role is, to monitor neighborhood groups. I oppose that. Neighborhoods respond to themselves and to the process that is set up in the city. I don't think you would want that.

The truth is that whatever you imagine, I had a neighborhood group which was accused of being racist and was then tossed out of funding and the new neighborhood group funded. Only the old neighborhood group controlled the nonprofits by state charter.

Now, we have a problem here, folks. That does happen.

Maybe more significant, let me ask this question. The City of Minneapolis buys a boarded up building, tears it down, and sells it to a nonprofit. Does the action of the city to buy the building with its administrative staff, with its cash, which is all from the CDBG, count for the 25 percent or does it not count in the 25 percent?

I can see a nightmare of regulatory questioning about what does count and doesn't count as the 25 percent.

This happens in my neighborhood all the time. We sold the block to a nonprofit. Does the money spent by the government to buy the block count for the nonprofit or not?

Then you can ask a new question and a new question and a new question, and the only people who benefit are those who create more administration.

Mr. **Ray**. We could probably do that with every aspect of the program. We could just throw out question after question, and I think probably that would be good because if we were open to or directed to looking at how this could actually work out, then through a system of asking questions with the idea of coming up with some answers as opposed to killing the program, I think we would get somewhere.

Mr. **Scallon**. The point is the reason Minneapolis has nonprofits is they have more power to do things in the city. I keep saying instead of regulating. That is where we all come from. We regulate right away. Enhance, give them more authority, make it to the point where the municipalities like Minneapolis and the politicians who have been through three different mayors and many council members, all the administrations all support the nonprofits, nonpolitical, and the reason is they can do more than the government.

And I am not urging that the government should build new houses rather than having the nonprofits build new houses. The point is enhance it, give them more authority, make it intriguing so that rural Minnesota doesn't have the feeling that it has to have a nonprofit to do everything. While in St. Paul they may not, but we do. We desperately need our nonprofits.

So I tell you the best thing to do is enhancement and not regulation.

Senator **CRANSTON**. Let me say that this sort of an exchange is particularly helpful when we get different viewpoints.

Ms. Sause, were you seeking recognition a while back?

Ms. **SAUSE**. I was. A lot of the points that I wanted to make have been covered, but Ms. Kelly I think really hit on the point that I wanted to get at.

We have had the funds decreased from 1980, when they were $3.7 billion. We are now hoping we get $3 billion. Inflation and added activities and communities have taken this toll. So there is more and more scrapping for fewer and fewer dollars.

And the thing I am concerned about is that the nonprofit community and the others we look upon as our friends and advocates to assist in getting the program funded are proposing significant changes to the program that will hurt local use of CDBG, and I hope we don't break apart on the rock of who gets what mandated funds.

So I really wanted to call on us to unite around Ms. Kelly's point and disagree on how the services are delivered because I think there are some good ideas here on how the nonprofits could have strengthened access without having the mandate that requires every community to use a prescribed method of allocating their funds.

Senator **CRANSTON**. Yes?

Mr. **STEWART**. Senator, may I just affirm that same point that Ms. Kelly made. We have really seen a 53 percent reduction in constant dollars. That really has simply thrown us all into a smaller bull pit, and we are eating each other up on that point.

I have some strong concerns that as we begin to mandate and include even more nonprofit groups, we are going to ruin our capacity to deliver small cities grants which many urban counties do. It is not so much urban county versus the nonprofits, but many, many small cities get their delivery service from that larger umbrella. They won't even be in the action if we begin to earmark or require that a certain percentage go to nonprofits.

Senator **CRANSTON**. Ms. Melkonian.

Ms. **MELKONIAN**. I also wanted to associate myself with Ms. Kelly's remarks.

I want to point out two other pressures that we know result from a lack of funds. That is, the shortage of funds has put more pressure on cities to make the terms of CDBG loans less favorable; in other words, to recoup the funding quicker.

The second thing is the reluctance of a city to concentrate enough funding in a particular neighborhood in order to have an impact because the city would be using such a high percentage of all the funds available in one place. So the funding question, I think, is really the priority question rather than the means of delivering.

Senator CRANSTON. Yes, Mr. Ray.

Mr. RAY. Might I say that I am representing the Coalition for Low Income Community Development, which represents over 700 organizations across the country, and we of course support an increase in funds for CDBG. We have called for at least $5 billion in funding for CDBG.

But the reality is that as we have seen the program's funds diminish the first groups of people or groups of organizations that have been crossed out or X'd out of the programs have in fact been nonprofit organizations, and we for that reason feel very strongly that 25 percent should in fact be in there. If we can move together to increase it, then that 25 percent shouldn't hurt anybody too much. I don't think so.

Senator CRANSTON. Yes?

Mr. ANDERSON. Just one bit of our experience in Los Angeles. One of the things we have tried to do in the last year or two is to substantially enhance our nonprofit delivery capability. We have got an interesting dilemma. We are considering the possibility of having a special set-aside or a special targeting of our housing funds associated with community development block grants and we have got the dilemma of are we trying to target nonprofits.

Well, maybe not. Maybe that is not what their objective is. In the State of California a nonprofit is simply an entity legally that can't issue stock. So that is not what we are talking about. We are talking about perhaps neighborhood-based nonprofit organizations.

Well, the mere fact that it is located in a neighborhood does not necessarily mean it reflects the needs, the interests, or the direction of that particular neighborhood. Quite often, a neighborhood-based organization reflects the interests of the executive director and the survival of that organization in the context of greater funding concerns.

So as we continue down that road, we have really ground to a halt, frankly, in trying to find what a neighborhood-based, neighborhood reflective organization is defined as being and how in fact we would set aside a specific type of targeting or funds for those organizations.

So we ended up looking at our delivery systems and public service programs. We have 147 deliveries. 95 percent of those deliveries are nonprofit. They are housing rehab, single family, multi-family. We started out with all 20 different areas operated by my staff or department. Now, only 12 of those areas are operated through our staff. The other areas are operated at the neighborhood level through nonprofits.

So we developed the capability there and turned it over to the nonprofits.

In the area of new housing construction, where we use block grants for gap financing and land acquisition, and so on, there is almost no delivery capability in the City of Los Angeles on behalf of the nonprofits, which is why we mentioned we served the nonprofit housing innovation fund to try to deal with some of the impediments in nonprofits in that area of the city.

But again we have got a unique local situation that we have tried to adopt uniquely, using the flexibility of the block grant. That is again why we want to maintain that flexibility.

We have a strong history in support of nonprofits. In fact, 270 projects have been done by nonprofits. And we also have the problem of that being the 25 percent. Making that the objective as opposed to delivery of services concerns us.

Ms. **Kelly**. Senator, I just want to make the point that if Mr. Ray is correct that nonprofits have been the first to suffer, I think that would be a tragedy, and I think anybody who doesn't have a nonprofit or doesn't work to support it in their community is crazy. There are things that nonprofits can do for the city, with the city, that no one else can do, including leveraging private dollars. There are many private sources that are dying to work with the nonprofit network.

So I again simply offer sincerely to talk to anybody who would like to have one.

Senator **Cranston**. Let's address the next topic, which is targeting, and our thoughts on that. We have just discussed the appropriate targeting of CDBG funds to low and moderate income persons is an ongoing concern.

In 1983, Congress required that each community target at least 51 percent of the CDBG funds for activities benefitting low and moderate income persons.

In 1987, low and moderate income targeting was increased to 60 percent.

Some favor still deeper targeting. One proposal is that 75 percent of all CDBG funds should be used to benefit low and moderate income persons and that 40 percent of all CDBG funds be targeted to very low income persons.

It is important that the subcommittee have stronger views on both sides of this issue, and that is what I hope to get from you.

The basic questions are how well CDBG activity is targeted to very low income persons now and moderate income persons in your own communities and, so far as you know, in other CDBG communities? How would more targeting help—or would it hurt—CDBG succeed in meeting the national objectives of the program? If tighter targeting is required along the lines of the 75 percent/40 percent proposal, what kinds of activities would be likely to get more assistance? What kinds of high priority activities might tend to suffer? What are the risks in more targeting of the program?

Mr. Ray, it is your turn around the table, so let me go to you at this point.

Mr. **Ray**. I guess one point that we would like to clarify—in terms of that 40 percent, we are talking about 40 percent of the 75 percent being targeted, which doesn't translate into 40 percent of total funds?

Senator **Cranston**. Yes; 40 percent of the 75 percent.

Mr. **Ray**. I am going to defer that to Mr. Gramlich, who has been working with the Coalition for about three years and has been working primarily with the targeting.

Senator **Cranston**. Fine.

Mr. **Gramlich**. Historically, the neighborhood groups, low income people around the country, have found that the program is not very well targeted at all to low and/or moderate income people. Jurisdictions will report that they are benefitting—90 percent of their funds are benefitting low or moderate income people. That is in HUD's annual report. Jurisdictions would suggest that 72 percent of the money is actually benefitting low income people; that is, people at 50 percent of the area median.

But when you go to community organizations and talk to people who live in those communities and sit down with them and look at the grantee performance reports and point out the projects, the activities that are funded by CDBG, consistently people say that is not benefitting low income people, that is not benefitting moderate income people, and the numbers can be challenged across the board. That is why the coalition is supporting or encouraging increased targeting, both at the 75 percent level and at the 40 percent level.

Mr. ANDERSON. Could I ask for a clarification? I am a little confused.

Was the issue that somehow the reporting was not an accurate reflection of what is occurring, which would suggest that we need to review the reporting process and ensure that that is being done properly? It wouldn't necessarily follow that you then increase targeting?

I got lost.

Mr. GRAMLICH. The point is that after 1983 jurisdictions knew that in order to pass HUD scrutiny they would have to show that 51 percent of their projects benefitted low and moderate income people, and they would write the grantee performance reports in a way that on the surface might suggest that that in fact was the case. But when you talked to people who live in those neighborhoods, people who are very familiar with the communities, they would say that particular activity may be in, let's say, a neighborhood that according to the census is low and moderate income but the project itself, the preponderance of the benefit is not for low income people or moderate income people, it is for someone else.

And if there is tighter targeting, that would be much more difficult for jurisdictions to do that. That would give local citizen monitors greater encouragement, greater authority to challenge the assertions of the jurisdictions.

Mr. ANDERSON. I don't know whether that follows. If the difficulty has to do with the manner in which the reporting is done and whether it accurately reflects the targeting that is occurring, then you look at that reporting process and the definitions of it and you tighten that up.

But to further target to a higher percentage doesn't in any way impact the problem that you are identifying. This is my point. And if in fact we are not reporting accurately and therefore not meeting that 60 percent overall threshold, that is a very serious problem that ought to be addressed.

Mr. SWAIN. Can I just make two comments on this specific line of discussion?

From personal experience in the Buffalo office of HUD, under the direction of Joe Lynch, and his very competent monitors over the last 36 months have become more and more diligent about tracking the requirements on low and moderate income households receiving the requisite benefits.

So as far as I am concerned, this is also, I think, demonstrated across the country when you see monitoring letters as lengthy as 45 pages that Dade County received, I think, in 1988 in Florida.

Senator Cranston. Is that the record so far?

Mr. Swain. I don't know. That is the longest letter I am aware of at the present time. [Laughter.]

Mr. Swain. I guess the point is that our opinions are that the HUD staff, at least in many of the area offices, are very, very good at accounting for the national objective of serving low and moderate income households.

And I guess the second and the most important point of all is that Mr. Ray made, first, reference to the block grant as a political slush fund and Mr. Gramlich has suggested there are abuses. I guess for the record I would request that they give specifics so that we have something to look at because I believe that the way the reporting systems are done at the current time and the grant performance reports are done, and so forth, that if there are abuses—and certainly in a program of this size we are not going to deny that there aren't problems with performance—those ought to be specified, and I believe the way that the legislation is written now and the way that HUD is monitoring the program and reporting on it clearly those abuses can be rooted out under the current set of circumstances.

So I would ask for specifics when we use terms like "political slush fund" because that is very pejorative and I think it is unfortunate to be used without some specific examples.

I guess on the whole the Community Development Association does not have a problem with 75 percent targeting because, indeed, the program is already at that level, if not above it. Clearly, the HUD reports indicate we are above the 75 percent level. So we don't have a problem with that.

We do have concerns about the 40 percent targeting, not because of the principle of serving very low income families, but because of what we believe would be a rather significant nightmare of trying now to develop a whole new system of accounting, particularly when one doesn't currently exist.

I think, Mr. Gramlich, you suggested HUD is specifying current percentages being spent for very low income families. I am not aware that they have that data available.

But in any event, our concern is again one of reporting and also, more fundamentally, that if you are looking at 40 percent to very low income families, there is the risk of fragmenting the program and having one neighborhood become competing with another, depending on what the census track data shows for median income, and again I would have to go back to the whole philosophy of flexibility, and so on.

It also suggests that at 40 percent we are starting to get to an anti-poverty program and back to a categorical program, which is as I alluded to earlier. The history of this is it is a block grant program, not a categorical program, not an anti-poverty program.

Senator Cranston. Yes.

Mr. **Gramlich**. The history of the program is also that the program is to principally benefit low and moderate income people. That has not changed since 1974.

Mr. **Swain**. Sure, it is.

Mr. **Gramlich**. We see consistently the fractious nature that you are afraid of. However, it is affluent people versus low and moderate income people. We see moderate income people already displacing low income people, and so I think the historical aspect of this is the amount of money that each jurisdiction gets is based on one of two formulas, and those formulas are weighted very heavily on the amount of poverty, the amount of overcrowding in the housing, and the amount of unemployment in the community.

So to the extent that you get as much money as you do is dependent upon very poor people and the awful lives that they are forced to put up with because of poverty. To deny them a modest access to 30 percent of the money, despite the fact that it is coming based on their very existence, seems to deny the fundamental purpose of the act itself.

Senator **Cranston**. Mr. Stewart.

Mr. **Stewart**. Thank you, Mr. Chairman.

To answer your question directly as put, 84 percent of all urban counties are targeting 90 percent or more of CDBG to low and moderate income populations, and I think that is a startling figure in light of some of the things we hear from time to time, 84 percent targeting over 90.

The other observation——

Senator **Cranston**. Do you think that we don't need to specify any targeting?

Mr. **Stewart**. Absolutely, sir.

Also, I would underscore we now have a block grant program. Let's keep it block rather than categorical. That flexibility that you have heard at this altar today is very, very critical to us. To try to track dispersed populations in some of these communities and seek the same ratio would be very difficult.

Our guess is, although there is not good data—I don't know of anyone who has good data—that they, too, are in that same category of 80 to 90 percent at least going to low and moderate.

Senator **Cranston**. Mr. Scallon.

Mr. **Scallon**. My question is, is that 45—40 percent of the 75 percent—we hear all these numbers. Some of us are just getting boggled. 25 percent set-aside to nonprofits, 30 percent set-aside to the 40 percent. Who can administer this?

I mean, we already had to hire a special staff person to administer the Barney Frank amendment. That is now $30,000 or $40,000 in Minneapolis that is going to be spent on the staff person to administer the Barney Frank amendment.

Now, this year we have a new amendment. It does cause me concern.

Let me give you a little broader view. I am again very prone on profits. They bring a lot of assets, but there are also neighborhood groups, and they take a neighborhood perspective. One of the objectives of community development block grants is the whole neighborhood. Some kinds of neighborhoods want to be a cross-section of folks, and they would like that project in their neighborhood for their cross-section.

What I just argue is that by the time we are done getting down to just serving low income and making this a categorical program you don't deal with the community as a whole. You don't worry about the housing structure, some of those things—age of housing, which is a standard. Community development block grants is larger than a small perspective. I think we have got to also remember—I have never forgotten—whenever municipalities fight the policy is to say, fine, we don't need that program. Pretty soon that program doesn't exist.

The policy that I am talking about is Section 8, new construction. Unfortunately, it doesn't exist right now, but the reality—and I thank Senator Cranston for all his efforts in housing—is that we really need a housing program that also needs working on. That is my argument. We have got to get back together instead of dividing up that very small pie that just can't be regulated and won't make a difference by the time it is done because we will be regulating such a small number.

Senator **Cranston**. Yes.

Mr. **Middleton**. I am just an old country boy, Senator. My rationale for all this is if it ain't broke don't fix it. We can all tell horror stories about how the poor aren't receiving the services, and it is all anecdotal. The fact of the matter is that when we view the history of the state administration of the program, the numbers way exceed 60 percent.

We are in favor and agreeable to changing the way the accounting is done, so that it isn't looking at whether the dollars meet a particular national objective. That would make sense to us. We don't have any problem with that sort of thing. But to the extent that you increase targeting in any way, shape, or form, trying to measure impact in rural areas, the net effect of that will be that it will be more difficult to meet local priorities. It will alter the flexibility of CDBG, and it will lead most of the states to allocate a higher percentage of their funds for housing rehabilitation in order to get the numbers up, and the issue in many rural areas is that it doesn't make much sense to have a nicely rehabilitated housing when they have no drinking water or where the sewer facilities are nonexistent.

And there is a side issue to all of this, in at least our experience in the rural areas, that even if you change the targeting provision it still doesn't address the issue of where the resources are really allocated.

In our own program we more heavily subsidize the very low income. If we are helping the community make water system improvements, we probably have to have new yard lines and/or plumbing in the very low income houses. On any kind of a proportional basis we are making a large investment in the very low income, but this accounting method wouldn't even capture that sort of thing, and I would really hate to be in a position where we would have to start creating or generating or keeping track of larger sets of statistics which becomes administratively inefficient.

Senator **Cranston**. Any more on this?

Yes.

Mr. Ray. I guess on two points. I guess if all low income people left the cities, then there would be no CDBG going to the cities. So we are talking about a basic equality of right and in some ways inequities. You are only talking about 30 percent.

The other thing, why this coalition has been very strongly behind targeting, is that several members of the coalition met with Congressmen and Senators and the concern was on their level targeting. In the past it has been used to cut CDBG funds. I don't know what the situation is today. Hopefully, that has changed, but the reality is that there is a need out there for those 30 percent that we are fighting for to ensure that they get CDBG funds and that there is no numbers game.

I am confused about people being brain damaged about being able to track the difference between 25, 40, and 70 percent, or what have you, when we have to deal with those things anyway. We have been dealing with reporting to HUD on numbers. We have kept in our minds the alphabet soup. We have planners that have gone to school do this. I really don't see a problem.

The simple fact is that we are talking about the basic rights of a program that is designed for low income people, and we are talking about the need to assure that the benefits are in fact there and that they are in fact real.

Senator Cranston. Mr. Gramlich.

Mr. Gramlich. Senator, all the Coalition is proposing is that 30 percent of the money be set aside for low income people. That means 70 percent of the money can continue to go to middle income people and affluent people.

My second point is if jurisdictions are in fact already devoting 80 to 90 percent of their CDBG money to low and moderate income people then they should have no qualms about there being something in the legislation that is far below what they are already doing.

Senator Cranston. Mr. Swain.

Mr. Swain. Yes, to Mr. Ray if I may. His reference to the fact that members of the Congress, House and Senate, are interesting in targeting and that is one of the reasons the Coalition has the proposal, I guess again I would ask for specifics because I am not aware of any particular evidence of that.

And more specifically, let's keep in mind that assisted housing, which is very targeted, has been cut by 80 percent or 70 percent over the last 8 years by Congress or by the President's recommendations and then overall the severe budget problems.

So I guess I would want to know what the specifics were and not just a reference to a meeting with members of Congress.

Just who are they who are urging targeting on your low income coalition?

Mr. Ray. Do you want me to provide that right here and now? Give me your address and telephone number, and we can sit down and talk about that. I will be glad to send it to Mr. Cranston.

Mr. Swain. Thank you.

Senator Cranston. Mayor Sarault.

Mr. Sarault. Very briefly, from my mayoral point of view, the targeting along these lines, especially the statistics on percentages that we have heard this morning would prove most frustrating to the CDBG objectives. We have in the community development block grant program very high percentages in this area and, keeping in mind the extremely small financial federal assistance we are receiving these days, obviously every community has a unique set of needs. I think flexibility is once again essential to the success of the program.

Senator CRANSTON. Mr. Anderson.

Mr. ANDERSON. We tried recently to further refine our targeting for block grant funds to the very most distressed areas, and we did our data cast using the 1980 census, and we began to have problems. The problem was, frankly, that the 1980 census, which is now a decade old, does not really reflect the realities of Los Angeles with respect to the East Side and the South Central Watts area. Radical changes have occurred in income and the resident profile that aren't reflected in the statistics, and one of the problems we have in reporting block grants, we were showing testing for low and moderate income and using the 1980 census data to support and substantiate that service to the low and moderate income population, taking that thought and applying it to the use of 75 percent and a portion of that. Currently, the city serves 86 percent of its clients, low and moderate individuals, and frankly it would be a heck of a lot higher if we weren't using slums and blight as part of the rationale for some of our urban development efforts. We are probably about 97 percent in reality.

But once you then take 75 percent set-aside for low and moderate income individuals and then take a proportion of that and we start applying that to an area, a benefit test, using the 1980 census, we are very concerned about getting it down to that finite and analytical point when the data simply isn't there that adequately reflects our reality in the city.

So on the 75 percent, we are doing it, we don't have any problems reflecting that. We are concerned about again becoming more categorical. But if the issue is one of the good intent of the people operating the program, 75 percent is fine because we do it. But to further refine that, we simply don't have the data base to be effective, and that is why the city has put off redefining its whole allocation process until the 1990 census.

Senator CRANSTON. Monsignor Linder.

Mr. LINDER. I believe that in principle the program is meant to target and that is all we are talking about now, defining, targeting. If some people speak on behalf of flexibility, I guess I am more concerned since it indicates that they don't intend to target the low income, which is the intention of the legislation. I think it is a matter of national scandal. I came from a city where the existence of low income people is used to justify the funds but at times the money is used differently. While Newark is in hard financial straits with large concentrations of very poor, it is understandable that the city might want to use the funds to promote gentrification or improving the city corridors so that vacant land can be marketed. While this approach is understandable, it does not benefit low income people.

So why not define what targeting means and why not enforce it, and why not say, no, there isn't flexibility there?

This is the intention of the legislation.

Senator **Cranston**. If there is no more on this topic, let's move on to the next area, another issue that is as controversial as targeting.

The Housing and Community Development Act of 1987 requires that the CDBG have an anti-displacement and relocation assistance plan. The provision requires persons displaced due to CDBG-assisted activities are adequately housed. Many localities and States have balked at that provision saying the cost of it will make it nearly impossible to engage in neighborhood revitalization.

So let me ask what has been your experience with the anti-displacement requirements? Have community development activities been held up or prevented because of them? What do you believe constitutes indirect displacement, and how would you propose ensuring that displaced families are adequately housed as government facilitates the urban revitalization?

Mike Stewart, we will start with you.

D. MICHAEL STEWART

Mr. **Stewart**. Thank you, Senator.

As an association, we have great concern that we have two masters. We would like to see all the displacement provisions focused under a single uniform relocation act. We have local governments that are, in effect, avoiding these kinds of projects for fear of the litigation that could ensue after they have identified a certain population, having an obligation for 10 years to have sufficient money in their budgets to keep them at a reasonable and affordable housing level, rent level, particularly when subsidies have eroded over the years.

So I think there is a deep, ingrained concern not to create a category which covers indirect displacement.

I think again some of that question is that local governments cannot be held accountable for the indirect displacement, which would discourage, we think, public officials from undertaking an effort to preserve lower income units. That is a market force phenomenon. To hold us accountable for that, particularly when there are no longer the subsidies available, as you are well aware, is simply a task we are not up to.

Thank you.

Senator **Cranston**. Any more on that?

DAVID N. LUND

Mr. **Lund**. Senator, if I might. David Lund of the County of Los Angeles.

Over the last 8 or 10 years we have seen—and it has been referenced many times around the table—a continuing restriction, tightening, strangling from time to time of the CDBG program.

Clearly before us here is another case in point. I would not presume to try to define indirect. Clearly, Mr. Stewart made the case that there are many forces outside the control of local government jurisdictions which, because of indirect—however it is defined—could well make it virtually impossible to practitioners like ourselves and local elected officials to deliver the programs that are so desperately needed out there.

So I would encourage you and urge you to stay away from and not retain this notion of indirect displacement.

With respect to the issue of two masters, I think it is a good analogy. The Uniform Relocation Act has been employed well over the years, and now truly we have two that we are confronted with, and I think what we are seeing is that communities are in fact staying away from their obligations and their responsibilities to do the job they need to do because it is too expensive. The private developers will no longer be interested or are not interested in working with communities because they know the costs of displacement and relocation are so burdensome as to be unworkable from the standpoint of economic feasibility.

So this whole issue is making it not only difficult but next to impossible to do economic development in our communities.

Thank you.

Senator CRANSTON. Yes?

Mr. SWAIN. A general comment first about experience with antidisplacement requirements.

I generally would say that the changes that have been recently made certainly provide more equity for the families that are relocated in whatever the activity is concerned; in particular, the replacement payment for up to $22,500 if the homeowner is relocated and the value of their home is less than the cost to them of acquiring a comparable unit. The replacement payment provision I think is an excellent one.

The concern we have with the current regs is on the one-to-one replacement. We are about to embark on a significant school project, in fact building four new schools in the City of Rochester, and the mayor and the president of the city school board specifically decided to put community development funds into those four new schools and related costs to those schools so that the relocatees would in fact be eligible under the federal guidelines for relocation.

So I think that is clear intent on the part of our people to be supported in the area of relocation. However, in working with HUD on it, it is unclear to us at the current time just how HUD is going to interpret the one-for-one replacement question. However, we are also prepared within our means to carry that out obviously as part of the federal requirement.

One of the issues clearly here on relocation and the one-for-one replacement question is that there are no funds provided, or certainly we have found massive cuts in federal funding for housing. So you have a one-for-one replacement requirement, but you don't have any money to go with that to provide for the one-to-one replacement. That is the problem.

In New York State we are very fortunate because the State of New York has very aggressively pursued housing initiatives. We have an affordable housing corporation for home ownership and we have a housing trust fund for rental purposes. So we are very fortunate in New York State to have state funding that can assist us in the one-for-one replacement requirement.

But that is a problem. I would urge that before we go any further on dealing with the topic of indirect displacement that we need time to fully digest and understand how we are responsible together, locally and federally, for the implementation of the current changes or the recent changes in the federal relocation requirements, so that we should not go further in now talking about indirect displacement. That begs the questions and concerns that have been raised already about the difficulty of defining indirect displacement and the like.

We ought to stand where we are and be sure that everyone understands how to implement the current regulations before going any further.

Mr. **Gramlich**. In 1987, when the housing legislation was going through, it was claimed that the CDBG program did not contribute to any kind of displacement. Subsequent to the enactment of the law there was a set of hearings on the House side and the Coalition, with very little effort, was able to present 29 cases in 21 different cities demonstrating direct displacement assisted through the CDBG program.

One of the arguments then was an argument that I believe Mr. Lund made today; that is, that this provision makes it too expensive to do economic development any more.

The retort of the low income people who were at the hearing who have been displaced was that why should a program that is supposed to benefit low income people harm them by making them pay the external costs of doing economic development. As a result of CDBG's activities, people are paying more than 50 or 60 percent of their income for rent. They are doubling and tripling up. They are being forced to vacate their apartments a couple of times. Homelessness is increasing. Congress is trying to allocate more money for homelessness while another program is contributing to homelessness.

It was asserted that there are no funds available to meet the one-for-one replacement requirement. Well, there is the CDBG program, and I guess a final retort to the "two masters" argument, the Uniform Relocation Act procedures and the CDBG provisions, is that also coming out of the hearing was that the URA did not work in instances where the CDBG program was involved, and to the extent that litigation with Legal Services attorneys tried to assist people displaced, the amount of URA compensation was totally inadequate to keep people whole for more than six months to a year.

Ms. **Sause**. My impression of those hearings was slightly different. [Laughter.]

If I might, I would like to dwell on that.

Senator **Cranston**. Go ahead. [Laughter.]

Ms. **Sause**. The URA had not been modified for years, and the need for it was overwhelming, and that overhaul did occur.

Before the overhaul and its impacts could be put in place, there was the drive to do additional requirements that would meet anti-displacement, perceived or real, problems without evaluating what the URA impacts and implementations would be.

I would like to just comment that in our city, San Francisco, last fall I set out to buy a small hotel, 27 units, occupied by 12 persons. The purpose that we were going to use that hotel for is transition for the homeless, the mentally ill, and that hotel if I were to undertake it now I would not do. I just would not be able to do it. The money that we set aside to do this, the money that we came up with, including the relocation that we felt was necessary to do to meet the new requirements of the "two masters", we would not do this project again, and I think that is not atypical of what is happening in other communities, and I say that based on the statistics, that we haven't found communities who are using or doing any relocation or undertaking any tasks since then.

So we come back to the philosophical dichotomy we are faced with here. We don't want to hurt anyone, low income or any other income, in our programs and in our communities, but we have programs here which enable cities to treat their ills, if you will, on the development side, as needed, where they can go in and use their community development activities and programs, a meager arsenal of tools to address blighted areas and deteriorated areas that occur in cities. Just as sewers fall in, so do parts of cities need addressing.

So we have established programs that will treat those cases and we have as a matter of philosophy said that city's needed to do so.

What we are seeing now with some of these ratcheting down of the requirements is cities are going to avoid using the programs to treat those areas. Therefore, I would agree with Mr. Swain and the others who say wait and see what the impact is on what we already have. To try and ratchet down the anti-displacement, direct anti-displacement any further I think would completely put these kind of activities to a halt.

I also think that if we start dealing with indirect displacement that we are going to open a can of worms that no one is going to be able to quantify or resolve the lawsuits that will evolve from that because philosophically there is some indirect displacement that simply occurs through the market intervention in the marketplace and other factors in cities, whether it is job loss or what it is.

So I just would urge that there not be further anti-displacements or direct/indirect anti-displacement measures until we assess the impacts of what we have.

Senator **Cranston**. Thank you very much.

Could we get on to block grants in another context, HOP?

Thirty-six percent of all CDBG dollars were used for housing related activities. Most of the housing related CDBG funds are used for moderate rehab, although some are used for substantial rehab. The HOP program contained in the Cranston-D'Amato National Affordable Housing Act will renew the federal commitment to affordable housing in a way that we hope will enable the CDBG program, among other things, to meet other community development needs.

So the question is what other necessary activities have been forestalled in the last eight years because CDBG was forced to fill the federal void in housing assistance? How should CDBG funds and HOP funds be used together? What protections should be placed in law so that the combination of CDBG and HOP funds doesn't lead to the provision of excessive federal subsidies to one development?

Could I start with you, Mr. Lund?

Mr. **Lund**. One of the concerns, if I might address it out of order, is the zero sum concern with respect to the funding. Given a finite amount of revenues to be made available, will HOP and CDBG, in competing with one another, does that mean a diminution of CDBG funding? That is not clear.

Also, I think what needs to be addressed—and we need some assistance on this definitionally—is how CDBG and HOP are going to be linked together. That has yet to be addressed or spoken to, and it is not particularly clear. I think from the standpoint of the HOP proposal new construction would be greatly facilitated and enhanced.

Senator **Cranston**. Let me say that we are not envisioning funding HOP out of the CDBG.

Mr. **Lund**. Thank you, Senator. That is great. [Laughter.]

Having new construction clearly is the key in the HOP program because of the significant, dramatic, stark cutbacks in new construction funding in housing over the last eight years. It offers new hope in an area that has been sorely lacking for some time.

Mr. **Scallon**. I am excited. My city has begun a dream of a 20-year plan of annual budget increases using local money, hopefully more federal money to really do the housing stock.

Let me just say after all this contentiousness, the idea that cities are getting better, and so forth, is just ridiculous. We are not any better. Gentrification is the least thing on my mind. I have got bad news for you. I wish I would see some somewhere. I see degentrification. I see folks leaving my city, moving to the suburbs, and housing stock going down. I see an increased area of need for housing. I see moderate income people replacing middle income people. The great fears I hear don't really exist in my neighborhoods, and I say that with all openness to everybody.

We are going to need more money to help provide affordable housing for first-time home buyers to moderate income families and to low income families for them to move out of being low income.

I am very excited. Our state in their graciousness has given us a few million dollars of money, and we combine that with the federal dollars, with our tax increment, which is a local resource, the property tax dollars, to provide affordable housing, but we in the late '70s had about $80 million in the City of Minneapolis—the state and local government and federal government, especially the federal government—for our neighborhood revitalization. We now have under $35 million, and I am including everything, including Section 8 subsidies, everything. We are trying desperately to go back up, and we have found $10 million I think in the near future of local resources. The state has given us 3 million. We really desperately need to combine them with all these programs.

How to keep this from being subsidized excessively is a difficult question because none of us ever realized how much Section 8 meant until we didn't have it. You don't know what you had until you don't have it. We have calculated it was worth 30,000 to 40,000 per unit on our development strategy.

I don't know if that is the biggest concern. My concern is we cannot produce enough affordable housing and still have enough housing, given that I have to face the reality that degentrification is an issue in my community, not gentrification. The reality is that there are people with less incomes in homes that used to have middle income families. Now, it is a moderate income family. If it is not a moderate income family, it is a low income family.

So I am excited about HOP. We will if we get such a program find the most innovative ways in our city to combine the resources, and I urge it forward.

Senator **Cranston**. I appreciate your enthusiasm about HOP. I hope that is shared.

Yes, Mr. Stewart.

Mr. **Stewart**. Mr. Chairman, just three brief observations.

We see HOP as putting housing back where it ought to be instead of in CDBG, which is neighborhood revitalization and infrastructure. You have got a great marriage there. At least one-third of all our CDBG monies are going now for reconstituting the housing stock or underwriting some 202 type projects. So you have at least one-third more money going into infrastructure for neighborhood revitalization. If we didn't have to use CDBG for housing—and we have three times more requests for CDBG money than we can possibly fund—that would probably be an easy rule across the board. Those projects are now going untouched, and it would enable them to be put back in place.

Senator **Cranston**. Any more on this?

Yes.

Mr. **Swain**. I, too, share the real enthusiasm over the introduction of the concept of the HOP program, certainly our enthusiasm over knowing that it will not cause a diminution in the funding of the community development block grant program.

As to the specific questions: What activities have been forestalled recently? I think clearly we in our community development program are not spending as much as we could be on human services programs. We are below the cap on that. Clearly, that is because we have put so much of our funding into housing, and also therefore we are relying on the United Way agencies in Rochester, and in our case the county does a great deal there. They are the primary deliverer of human services. What would we do if we had not been doing so much in housing that we believe the federal government should be doing?

Public improvements in qualifying neighborhoods, park improvements, street work, sidewalks, curbs, trees—these kinds of public improvements are very, very important, again, to the overall neighborhood revitalization strategies, and we have specifically two years ago stopped doing those with community development funds.

That is another indication of an activity that we had foregone, which to many people is very, very important in their neighborhoods. As to the question of excessive federal subsidies, that also obviously, as has been said, is a difficult question, but I would point out as the public housing program currently exists—and it, too, should be expanded, incidentally, and very importantly—that provides the capital funds for constructing the unit. Also, it provides for operating funds to the PHAs for operating public housing. Those subsidies are very, very deep, as they must be by necessity.

I don't think there should be concern for excessive subsidies to the housing development except that obviously the housing that is done through the HOP should be—as the proposed legislation provides—it should be targeted and it should be based on the substantiation of the household incomes that these subsidies and the depth of those subsidies are ultimately determined. The lower the income, the deeper the subsidies.

I find myself in talking to HOP being on the side of targeting, and I appreciate that there is targeting in the proposal currently, but in this case, rightly so, there is targeting because this is a housing program, so that we have no problem with the targeting.

In fact, a year ago we were concerned that there was not targeting in the proposal at that time.

Ms. **Kelly**. Senator, so many of the arguments strike me as being sort of crabs struggling in a barrel. It is an issue of how few resources there really are, and I guess how valuable the CDBG program is—I am really encouraged to hear that it is not your intention to cut it. When we talk about communities, we are working in communities around the country—in Bridgeport, Connecticut, in Jackson, Mississippi, and in Oakland, California—and it strikes me when I think about Stamford, Connecticut, which everybody assumes to be a wealthy, affluent city, there are many families in Stamford who make combined annual incomes under $15,000. If those families are displaced, there is nowhere within 75 miles for them to go.

CDBG dollars enable most of those families to keep their homes, and they do make a difference. The same is true in a city like Lawrence, Massachusetts, where two-thirds of the revenue in that city comes from public-federal-state assistance. We are working with the city government and a nonprofit there to put together a comprehensive homeownership plan for five neighborhoods in the northern part of that city, and without CDBG funds it would never have worked. The private sector wouldn't be involved, the state wouldn't be involved.

So I guess it is the glue that holds things together. It is a flexible fund that has been absolutely invaluable in every one of the 218 neighborhoods that Neighborhood Housing Services has been working in, and I would just like to emphasize that point.

Senator **Cranston**. Thank you very much.

Mr. Anderson.

Mr. **Anderson**. One other comment. In the city we have got a group of over 20 some percent of our citizens paying more than 50 percent of their income for housing. So even——

Senator **Cranston**. Say that again.

Mr. **Anderson**. Over 20 percent of the population of Los Angeles, 50 percent or more of their income goes to housing. So even with the Cranston-D'Amato legislation we don't see turning our back on housing block grants. Really, what we see in the block grant is a shift to much more emphasis on neighborhood type activities. This means neighborhood housing where we continue to do the small-scale rehabs, single family, multi-family, through nonprofits, and so on, shifting more of our housing production, new construction being driven through your legislation.

That really gives us two tremendous tools and focuses to do that, which then leaves us with some additional resources in the block grant to again support neighborhood activities. The essential neighborhood development that we need in such communities as Watts to drive any economic development has absolutely not begun in the City of Los Angeles. We have not begun to do it.

The whole issue of libraries. We have ceased funding libraries in the city as of this coming block grant year. So the whole issue of developing neighborhood libraries or literacy programs and the pressing needs that we have now, that has gone. The idea of creating neighborhood facilities for nonprofits where we have the ability to bring in operating funds from other sources, we can't do any more.

We can shift again the emphasis in neighborhood facilities.

So that is what we see happening if in fact we could have the new housing legislation, a reemphasis and a reaffirmation of the neighborhood activities under the block grants, which does include housing.

Senator CRANSTON. Councilman Scallon got into Section 108 a minute ago. I would like to get to that as it relates to the future of CDBG.

Presently, Section 108 loan guarantee programs allow local governments to pledge their community development block grants, as you all know, as security for a loan up to three times their annual appropriation. Some have argued that nonentitlement communities be allowed to participate in the program also.

The House passed appropriation bill now would cut Section 108 loan guarantees from 144 million this year—that is this year's figure—all the way down to only $46 million next year. The Administration tried to cut the whole thing to zero.

The questions on this topic are for what types of projects has the Section 108 guarantee program been most helpful? We need that ammunition to try to defend it. How might the Section 108 program be used in the future? How easily could states pledge a portion of the CDBG allocations as security for the localities' needs and, just generally, are there any suggestions of ways to improve and strengthen Section 108, if there are ways of defending it?

I would like to start with you.

Mr. SCALLON. One of the interesting things about Section 108 is that my city tried to use it and decided instead to be creative and fund a large project and take down the monitoring of the federal Treasury with our existing money, and I know—I would hesitate, Senator, but I will make a suggestion because I noticed the OMB is more powerful than all of us in this country—but if there could be a way that when we took down CDBG, if any interest income or any benefits could go for a housing program as part of it, it would just be really neat.

We decided we had a problem we couldn't solve and we took down—we switched our money sources around and took down our money early, bought the blighted block. As it pays itself back—it is downtown, so it can pay itself back—we will go out and do our neighborhood projects.

So we are in effect helping a blighted block downtown without taking away from low and moderate income housing, which is one of our goals, and we did it with HUD approval, buying down all the community one block earlier.

Section 108 would be a very creative section for all of our procedures. I see it as a way to buy and do large projects in small cities, and I see it as a way to do some creative kinds of rehab loans that could be created through it. I do say that we will be in desperate trouble in our communities if we don't have access to that. I think one of the ways we are going to be able in the city that I am from to use 108 would be to borrow 108 for rehab loans for bigger projects and make sure the money is then repaid into the project and be able to continue on.

By just taking down our existing resources in my city, we were able to help a terribly blighted block without hurting anyone in low and moderate income.

Senator **Cranston**. Yes, Helen.

Ms. **Sause**. There have been a number of creative uses that Mr. Scallon has outlined by cities across the country, primarily to acquire land and to develop it using concentrated larger amounts of funding than we can predictably have in a CDBG year. You sometimes need something that gives you a larger chunk of money than that.

I know that in Kettering, Ohio they have used 500,000 to finance the acquisition of land there for a General Motors plant. They have done some things like that in Monterey Park, California, where they used their loan for $2.2 million to purchase real estate that would facilitate the development of an auto sales area, a retail area.

Those kinds of things have been used, but we have talked a lot about flexibility, and this is a program that needs the feature, also. It needs more than it has now. It is really needed to have the expansion of the time payback, and I know that in the bill that has been introduced by Representatives Ridge and Gonzalez and others in the House, H.R. 2779, there are a number of flexibility aspects to that bill that really help us in using Section 108.

In addition to extending the payback period, it gives preference to areas that have designated enterprise zones. Enterprise zones has been a rather hollow promise at this point. There is not much to it. Even in states where they forgive taxes or accrue benefits, it doesn't have much meaning.

Section 108 could be instrumental in helping give some teeth to that. I think there are more flexibilities that could be done, but that program is a very significant one and is a badly needed one in the face of not having a significant development tool now that UDAG is gone.

Senator **Cranston**. Yes.

Mr. **Anderson**. I would like to also add to that.

With the demise of UDAG it is very difficult for block grant operators to come up with a significant amount of funds to do worthwhile projects. There is only about one that we can do in the city now where we have a target. We have a $9.5 million one-way loan now that we are using for commercial development that will generate maybe a thousand jobs.

What we in effect did was use that $9.5 million as a permanent loan to the developer to allow them to take down land. The land has sat vacant for over eight years. The reason it sat vacant was that there were serious toxic problems with that particular part of it that were causing serious health concerns for the broader community as well.

In addition, the banks would not loan them for that property. They were loaning approximately 62, 63 percent of the overall project cost. The developer could not come up with 37 percent of the project cost up front. With our coming in with that particular amount of funds, it showed the development community that we were very serious about standing behind them, even when we had a toxic problem.

In consideration with that, we had a direct linkage with the Job Training Partnership Act; 60 percent of the people we were hiring came out of the JTPA directory. So we were able to get a very, very strong commitment from the developer as a result of that large chunk of money we were able to put in. I guarantee we never could have put in $9.5 million of a $55 million block grant for a single project in a single area in the City of Los Angeles.

So that program I think is very, very critical.

Echoing a couple of points about the expansion of the flexibilities and some of the things there, expanding the payback term for 6 years to 20 is very critical. Six years is the minimum amount of time that you can even have a reasonable discussion with a developer or business person about a loan period. Again, that is almost too short a window. If you figure a construction time of approximately 2 years in addition to lowering the cap to some $47 million, it would make it unusable nationally if you had any significant draws on the funds.

Also, expansion of the kind of activities with which you can do runaway lending would be helpful, and we would like to explore that in some other areas because as resources become more limited we are looking ever more so at the kind of creative things we can do with what is left on the table, and 108 is one of those things.

Mr. GRAMLICH. I would be the first to admit that I do not have much depth of knowledge about Section 108 programs. So let me ask two naive questions.

Back in 1983 HUD took a look at section 108 and did a study. Before Congress acts dramatically on section 108 we might try to repeat that study, and one question I have based on that 1983 exercise is how do you determine to what extent projects that were going to be funded out of the payback that is going to come from project revenues turned out, due to project difficulties, to actually come out of CDBG money; and to what extent was that problematic with the communities? Back in 1983 that was at 12 percent. We can all judge whether or not that is reasonable or not.

Before we go on into the future, especially with UDAG being gone, I wish we would take a look at what has been happening since 1983 to see how much CDBG money might be jeopardized by projects with project revenues insufficient to make a payback?

Mr. ANDERSON. Is there any evidence of defaulting on section 108 loans?

Since we are talking about at risk, for example, in our city project, we have first position on the land and we also have full recourse to a letter of credit. So our position is solid no matter what occurs on the project. The problem there is that there is no income other than the absolute cash. Irrespective of the terms of the loan itself, it was coming up with the absolute cash. That is what the 108 loan did.

Mr. Scallon. Similarly, in our situation it is guaranteed that we spend our local sources of money in the development account and also a tax increment. The only way we could get rid of the big block in our city was to buy it and move it. That was the only choice. It was a commercial block, basically a downtown commercial block that had turned into a troublesome block, and it was destroying—a lot of the problems we're having were coming off that one block. It had the highest crime rate in the metropolitan area on this one block. It was ridiculous.

It is also part of an effort of ours to remove a blighted commercial area and then guarantee it with different kinds of things, and if you can't get enough cash from your other sources this is a good way to do it without losing an awful lot of income.

Senator Cranston. Yes?

Mr. Ray. Two concerns. One would take us back to economic development, which is important to us, and the other is the fact that there should be a requirement for payback and a requirement for payback outside of the CDBG funds.

For example, one example that I guess would be quite glaring in Richmond, Virginia, there is the use of a CDBG 108 loan and for the past 4 years off the top a small figure—of about $3.75 million, $689,000 came off the top to repay that section 108 loan. We think that that process actually hurts low income people.

But to go back to economic development, we skipped that part, and it is important for us. We have in most cities planning staff, yet when it comes to economic development and the use of CDBG funds for economic development there is often a lack of planning, which results in the use and sometimes abuse of CDBG funds.

The Coalition is calling for a required development strategy prior to any use of CDBG funds for economic development. Within that strategy we need to describe specifically how low income people would be benefitted. We need to describe specifically the nature and amount of the long-term employment that will be created to benefit low and moderate income people.

Again, we are requesting that because we keep seeing the use of CDBG funds in several projects across the country that touted very high figures of permanent jobs being created that were never created or that were created very temporarily, in some situations temporary to the extent that jobs lasted only for a period of one, two, or three weeks. It is important that we are going to use CDBG for economic development and that we do plan for it.

We have in all cities a very capable, competent planning staff who can plan everything else in the world. Why can't they plan economic development strategies?

Mr. Swain. Just a couple of different points for the record.

The Community Development Association certainly supports the section 108 program as being very important. We support the extension of term as important, as has been mentioned, from 6 to 20 years. So some of these flexibility points are critical.

One point at variance with some of the earlier comments, we have questions, I guess, more maybe the tactics or strategy that would allow section 108 to be used for housing because we would not want section 108 being used for housing and then have that be used as a rationale for not meeting a HOP program.

So the question is the prudence for including housing in the eligible activities in section 108.

On the last point by Mr. Ray, the Community Development Association does generally support the economic development planning language that has been referred to. We, too, believe that local governments have developed significant planning capacities, particularly because of the community development program over the years, and so the economic development strategy should be a part of that overall planning.

Senator **Cranston**. Mr. Finkle.

Mr. **Finkle**. Senator, I do want to go to the issue of economic development as regards the question—in fact, I wanted to respond to the question as it was asked, the first question on economic development; that is, for what purposes must CDBG economic development choose?

It listed a number of tools that were capable of being used for economic development, but I think the proper answer to that is for aiding low and moderate income people in finding and keeping employment in their communities is the proper response as opposed to whether it is a retention strategy or creation strategy or an attraction strategy for the community.

Economic development, part of the CDBG programs, must meet the requirements of the block grant program, and I guarantee you, as opposed to what Mr. Ray said, if HUD found that a job only lasted two or three weeks HUD would not go along with that meeting the benefits test within the economic development provision of the block grant program. Economic development is an integral part of providing low income jobs within many neighborhoods in this country, and it is an important part of the community development block grant program.

Senator **Cranston**. Yes?

Mr. **Gramlich**. First, I would like to commend HUD on their new regulations pertaining to the economic development provisions of the Act. I think that helps keep that particular activity on track.

The primary purpose of the CDBG program is principally benefitting low and moderate income people. Those regulations, as I understand it, come out of several Office of Inspector General studies that looked at the use of CDBG for economic development and found that the number of jobs promised were not nearly as high as reported, that those jobs were not necessarily going to low income people, that they were often part-time jobs, that there was very little reporting and accountability.

Now, I think we have got a mechanism there that can help us all feel comfortable that the economic development activities are meeting the objectives of the program.

Senator **Cranston**. Yes.

Mr. **Middleton**. To respond to the question on the Section 108 guarantees, the states have not been able to use that program at all historically. So we don't have any experience.

But the specific question was raised, how easily can the state pledge a portion? I think it would be politically difficult, for starters. Second, we will get four to five applicants for every project that we can fund. Most of our projects are project specific. So a community gets funded and they won't be back at the table again for a while compared to entitlement cities, which have a particular funding for a particular jurisdiction. We have no idea how or whether states or smaller communities will be able to use the program.

Senator **Cranston**. Yes, Mr. Finkle.

Mr. **Finkle**. Senator, I did want to respond in terms of new regulations that HUD has issued dealing with a block grant program in economic development. We have done a significant survey, and I have also provided a very long testimony to the committee which deals with the issue of economic development.

But we are finding that with the new regulations economic development is becoming increasingly difficult to undertake. We are finding that it is difficult to undertake in low income neighborhoods by minority entrepreneurs who are dealing with it as first-time business owners. We are finding it difficult to use for existing businesses, and we are finding it difficult to use in enterprise zones, which HUD has indicated is the target area for which they would like economic development activities to occur with the block grant program.

We anticipate a significant reduction in the amount of jobs that are going to be created with the block grant program. We see a significant amount of dollars that are going to be reduced, and overall I think that is going to reduce the community's ability to respond to the employment needs of low and moderate income people and communities as a result of these new regulations.

Mr. **Middleton**. I will raise a question about what would happen if increased targeting were to occur, particularly in economic development projects. I think if it ever got to the point where it was project specific it is difficult enough for most businesses to be willing to participate with all the red tape that goes along with any of these programs. If we increase the targeting levels, the only kind of jobs that we are probably going to get are going to be sweat shop jobs, which is counterproductive to the intent of the legislation in the first place, and they will probably be temporary jobs for companies that are either going to go out of business or are on their way offshore. Targeting in that level of program would just be counterproductive.

Mr. **Gramlich**. I would like to clarify that. As far as I am aware, there is no proposal to increase the targeting per se in economic development. It is my understanding that the current obligation of ensuring that 51 percent of the jobs are held by or are available to low and moderate income people would be constant.

Senator **Cranston**. Mr. Scallon.

Mr. **Scallon**. You can see what happened to targeting. Targeting is a surreptitious way of preventing economic development by CDBG. I understand that.

In our city we have a jobs program that really is related directly to the neighborhood. In other words, you have a neighborhood person displaced in a job and there is a contract for community development and everything.

But what I want to say is to the largest extent community development block grants is not just for the low income people. They have the right as low income people to live in the neighborhood. It is a cross-section of people. I just can't tell you how much the negative, blighted commercial block has on a neighborhood. I think as you focus your minds you are missing the point of development, the CDBG program.

Yes, it is for low income people somewhat. Yes, it is. It is broader than that. I haven't heard the breadth here, but I hope you do think about it, and that is that they have a right to go to the store.

Now, listen before you jump in because I can't resist this. We have a shopping center owned by the American Indian community. We have a job center owned by American Indians in my community. You know, if you put these same restrictions on them, their own program might not work, even though it is a nonprofit group, because they do have some troubles making sure they are meeting all the requirements. We do meet them.

But be careful when you leap in. Low income people have a right to live in a decent neighborhood that has the services that everyone else has. So as you put all your restrictions on, you ought to loosen them up just a little bit for the neighborhood commercial areas, which are not doing well in most of our cities, and all your restrictions I think will make it more difficult.

Mr. GRAMLICH. I don't think there are any particular restrictions we are talking about. We are just supporting the regulations that already exist, the regulations which were implemented because the program was not meeting its objective. It was not benefiting low income people, and perhaps what you are suggesting is that Congress change the law to eliminate the primary purpose; that is, the principal benefit goes to low and moderate income people. Maybe we should change it to say maybe it will benefit some people who might be displaced or people who might get a job or people whose streets and sewers might happen to go past them.

It seems that we are losing the flexibility for low income people.

Mr. SCALLON. I think you are trying to go the other direction. I don't want to get too deep into it. I think philosophically we feel we have a working capital program. We have a first-time home buyer, first-time jobs. We are flexible.

We keep coming back to flexibility. I would like to have more flexibility for commercial. Honestly, if you can't sell a blighted building you are not going to fill a home, and I have got news for you. Folks won't live long in a home behind a blighted building.

Taking a very insulated viewpoint with CDBG for the low and moderate income people whom I represent, what happens when a minority owned business can't pass your regulations that you are speaking so highly of? What happens when minority people are being excluded because they can't meet the regulations?

At least stop a second, step back, and say, yes, there are other things than economic development in the neighborhood that are also important. Having a decent neighborhood commercial area is important for low income people. They shouldn't all have to live next to boarded up buildings.

Mr. MIDDLETON. I guess I must react for the record, to strongly object to some broad, general, sweeping statements that economic development is not in fact benefiting low and moderate income people in the community development block grant program. All I ever hear is anecdotal evidence, horror stories that we could generate, Farmers Home could generate, EEA could generate, any program could generate, and the Inspector General's report is methodologically suspect. It was a hatchet job. It was dumb.

The fact of the matter is that the program's objectives are being met by economic development. It is not to be denied that there are some problems with the program, however. I don't want to see more red tape complicating our ability to do that, particularly in the smaller communities that don't have the same kind of opportunities for economic development as our larger urban centers.

Senator **Cranston**. Yes.

Mr. **Finkle**. Senator, the new regulations were talked about in glowing terms. Unfortunately, I think that we are just now recognizing the problems that those new regulations are causing in terms of the area of economic development, and it is my hope that the full committee will kind of ask HUD to relook at those regulations, acknowledging the fact that they have essentially made economic development nearly impossible to do. If that is going to take a statutory direction or legislative direction to the agency, that may need to be done, if in fact this committee does not want economic development to be eliminated from the block grant program.

Mr. **Anderson**. Senator, this is one of the subjects that defies the one-liners. It is very, very complex, and what is happening for those of us who are economic development practitioners is that the program is going to die in abating. It is a regulatory problem.

Let me just really quickly summarize it. In the City of Los Angeles we currently provide over 250 loans during the course of a given year. We use everything from 108 flow financing, SBA loans, state loans, block grants, we have got small business loans, gap financing, mini-UDAGs. We do extensive lending. We have a well-developed loan program.

The new regs that came out basically give you two ways to qualify. The job either has to be filled by low and moderate income individuals or be available, and the definition of "available" is very arduous and very onerous. So I just want to focus on being filled by.

In the past we simply had to show that the job requirements were such that low and moderate income individuals would qualify. Now, you have to basically certify their income. Our problem is this. In working communities, such as Watts, we are begging developers to go in there. We are trying to change that neighborhood. We are trying to bring an employment base in there, and it has none.

The difficulty is when you have a developer who is doing a commercial shopping center who refuses to commit up front on behalf of tenants which they don't yet have and they are very concerned about getting them in a distressed area, then in fact they will do a means test when they employ people, and also the means test—the benefit is not received by the employee. They are just out looking for a job and they are applying. It is not like a job training where I go apply for job training services and at the end there comes a job, and therefore I will give myself up to an income review.

If I am just a person aspiring for a job, I have got to have some sort of means test before I can even accept the job? That is causing all sorts of problems with the limited English speaking individuals that we have in the city, and particularly lower income jobs.

What happens is developers are very concerned about making commitments on behalf of the tenants they don't yet have. In addition, you have got primary users, such as manufacturers, who are also having to provide favorable financing to attract them into a neighborhood, who don't want to commit up front to those kinds of requirements.

What we would like to see, frankly, is a compromise between the two extremes. Clearly, all of us have an absolute concern that we would be able to document that low and moderate income individuals are benefitting, period. If they are not, we shouldn't be doing it. On the other hand, we can't have the documentation process be such that it kills our ability to do those economic development activities.

What we would suggest is this. In the situation where the business that you are assisting is in a primarily low and moderate income area, whether that is 51 percent or 60 doesn't really concern us because we only work in those distressed areas in our economic development, but where you have got such a census track in which the business is located and the job is appropriate for a low and moderate income individual, as in the old regulations, we would ask that on the face of it that loan be deemed eligible and appropriate.

In effect, what we are saying is we would like an area benefit approval for an economic development activity that is in an area that is low and moderate income, such as we have in other activities on the block grant. If we had that, what it means is on the face of it where we go into the most distressed areas, those business loans and development loans would serve low and moderate income people. If it is outside the HUD census track that is primarily low and moderate income, we fully agree that frankly they ought to be documenting that in fact low and moderate income people fill those jobs because it raises a lot of questions as to why in fact we are doing deals if the development is not in the most distressed areas.

The second thing that people have to take into consideration is that the development you are doing in distressed areas has all sorts of spinoff effects that are very, very critical. The mere fact that you have got an increased activity increases public safety. It provides additional spinoff and trickle down jobs. So there are a lot of things that happen in economic development activities in distressed census tracks that ought to be taken into consideration.

Again, just to summarize, rather than leave it the way it is now where you have to substantiate that each job is filled by a low and moderate income person, with all the onerous requirements that that puts on a business person, if it is in a distressed census track and the job is accessible to a low income person, on the face of it it ought to qualify.

That is what we would like to see.

Senator Cranston. I think we have pretty well covered the agenda that we have laid out for you in terms of the questions that we thought we should cover.

Is there anything that we should have had on the agenda that we didn't put there? Anything that you would like to add that we should be considering in terms of revitalizing communities?

Yes, Helen.

Ms. SAUSE. I guess I am feeling a fair amount of panic that CDBG has almost been the stepchild this year. I know Congress has put a lot of energy into solving the bailout of the savings and loans. For us the potential of not having this program reauthorized is a crisis, also, and to have it tacked on to whatever legislation we can get in 22 days remaining is something that is of deep concern to us.

I appreciate the roundtable, but I also need or hope that this committee will advocate for the reauthorization in some very effective way, but the GDBG program is part of a number of tools that are used to stabilize neighborhoods, and along with it we absolutely need to have restoration of the Section 312 loan program that goes to support the Urban Homesteading program, and we also need to have Rental Rehabilitation program.

Those programs are all needed, and we talk about the CDBG program. It is a workhorse, but without these other tools our programs are nowhere near as effective as they could be otherwise. So I really want to be reassured that in the next 22 days something is going to be done that gets the program reauthorized and that these other programs are being advocated for at useful funding levels as well, particularly 312, which has unfortunately been cannibalized for other purposes. We need to have 200 million restored to that program to make it useful.

Senator CRANSTON. Mr. Swain.

Mr. SWAIN. Just on the question of secondary markets for CD loans. We think that is a good idea. There are some problems now with the way the loans are structured, the different terms and loan positioning across different cities, but we think that the secondary market is a good idea.

On the more general plane, I would want to just summarize by complimenting you, Senator, for undertaking a hearing in this sort of format. I think these kinds of exchanges are very, very healthy and very positive. We also appreciate the work of your staff in putting together the questions, and we think that the airing of these kinds of issues which we have been hearing about, and talking about within our own organizations, the airing of them in this sort of forum is a very, very healthy process and hopefully one that can continue.

I would go back to some of the fundamental comments or concerns. One I think clearly—the point that Ms. Kelly raised initially about the real fundamental issue here—is funding and the real reductions that were mentioned in the block grant program over the last eight years of probably over 50 percent in real dollars, that is the real issue.

We think the community development program has been a very, very positive program during its life, a very good program, and as I said earlier, I think that philosophically we all in this room believe it is a very positive program that deserves additional funding, and as Ms. Sause has suggested, we are also concerned about reauthorization, obviously, as well as the refunding of the program.

With that, I thank you again for having us.

Senator CRANSTON. Thank you.

Let me say that we focused on housing legislation because housing policy was pretty well shattered in the last few years, but we have seen CDBG as a solid program that doesn't need any dramatic overhaul.

Is there anything else that you think we should have covered that we haven't covered?

Ms. KELLY. Senator, just let me mention briefly around the issue of secondary markets for municipal loans—Just for the record Neighborhood Housing Services of America has begun a pilot project on purchase of municipal loans. As we all know, it is a very difficult venture. Direct CDBG loans have historically been a source of last resort. But I think it is something worth pursuing.

And I would recommend that that NHSA pilot be looked at and supported to see where it leads. There is a great deal of learning that has gone on.

Senator CRANSTON. Yes?

Mr. ANDERSON. Not to upset the apple cart, but one comment with respect to the public citizen portion of the block grant that is currently 15 percent. I don't know whether we want to get into a discussion about changing that cap, but one minor modification I want to suggest, and that is for the grantees where they submit their application as both a basic block grant allocation and appropriate income and other funds that you are putting into your application process, we would like to see the 15 percent go to both, not just the base allocation of any program income that was generated the previous year that is going into your application.

We feel strongly that the City of Los Angeles should have the flexibility—because it is generating that program income from whatever source as a result of the block grant activities, that we should have the same flexibility to apply the 15 percent to that income as well. That would again give us more flexibility to address some of the pressing local needs that we have now, such as gang and drug intervention, where we are woefully unable to respond in any adequate fashion.

That is a regulatory change. It is fairly minor, but—there is no fiscal impact, but it again gives us more local flexibility.

Mr. SCALLON. That is one other thing, urban homesteading and the VA repossessions. So far the only Congressional interest is giving a few to the homeless, and they are fighting about that, but there is a bigger interest. Those buildings are a great opportunity to bring into the city and bring other folks back in. Somewhere in here it gets lost in free fall. There is just not enough 312, A10, and all the other alphabet soups that we have. Somehow or another FHA has to bring those repossessed houses into the whole neighborhood for community development strategy.

Ms. SAUSE. Statistically, the 312 program has supported the urban homesteading.

Senator CRANSTON. Anything else?

Yes.

Ms. MELKONIAN. I don't mean to seem facetious, but I do want to ask one question, and that is when are we going to get a peace dividend. Now that we have paid for everything, we are armed to the teeth, and our enemies have cried "uncle," when are we going to give ourselves a break and start reinvesting in people?

Senator CRANSTON. I hope soon.

I would like to ask Don Campbell, who is the Staff Director, as I think you all know, of the committee, if he has any questions that have come up that we haven't dealt with or any loose ends.

Mr. **CAMPBELL**. Thank you, Senator.

Certainly, no questions.

Senator Cranston several months ago launched this roundtable format for hearings, and I think today, at least in my experience, has demonstrated the value of that format as well as any. It was a terrific hearing for me, and I think it has been very helpful for an exploration of some very controversial issues.

Just to answer your question—I would assume it is a concern for other people as well—the expiration of the authorization is coming up. The precedent is that the appropriations action is its own authorization in the absence of the authorization. So I fully expect the appropriations bill will be enacted by that time. So there is no urgent need for authorization legislation separate from that, although we will be looking at longer term reauthorization of community development block grants, and discussions are going on already between the staffs of the Senate and House to lay that out.

Just finally, this is only one step in the process of coming up with that bill, and we are looking forward to working very closely with individuals around the table and the organizations that you represent to refine the existing legislation. This is the time to sharpen up your ideas and get those ideas in focus.

Senator **CRANSTON**. Do any of you have any questions for Don?

Ms. **SAUSE**. Just a comment. He has certainly done yeoman work in this whole long process of the HOP, and I think we all applaud him for that.

Senator **CRANSTON**. Yes. He has done very effective work. We owe a lot to the staff, and we also owe a lot to the regional task force that we had. I think they did some very, very hard, effective, and very creative work.

Yes?

Mr. **FINKLE**. Senator, I apologize for not raising this earlier. It is my understanding this afternoon you are going to be looking at Anna Kondratas, the Associate Secretary designee. I hope maybe you will note some of the wisdom that you have heard here today and maybe get the Department directed in the proper way in some of these areas.

Senator **CRANSTON**. We hope we can. I believe that Secretary Kemp is very intent upon doing a very creative job. How many resources he is going to get as far as allocations are concerned to meet pressing needs is not clear. Congress may have to provide the leadership. We will have to really see. But I know he is doing his best to do a good job, and OMB and other powers that be are there to be dealt with also.

You have helped make this format work very, very well. It has been very informative, certainly from our point of view, and I hope yours.

I thank you very, very much. We now stand adjourned.

[Whereupon, at 12:40 p.m., the subcommittee was adjourned.]

[Prepared statements of witnesses follow:]

STATEMENT OF

Jeffrey A. Finkle
Executive Director
National Council for Urban Economic Development

on

Community and Economic Development

before the

Subcommittee on Housing and Urban Affairs
U.S. Senate

September 8, 1989

SUMMARY

The following statement examines problems and complaints voiced by both the public and private sectors concerning Community Development Block Grant (CDBG) regulations specific to economic development. The chief concern among CDBG recipients is that the regulatory requirements, rather than the statutory intent, are determining what type of assistance is provided. This tends to limit rather than improve the effectiveness of economic development efforts. Issues covered include:

o Confusion created by the "Stokvis memo" of June 1987;
o Documenting low-mod family income requirements;
o Overly strict interpretations of the "necessary or appropriate" clause;
o Davis-Bacon demands;
o The limited focus of eligible economic development activities;
o The potential for a secondary market for community development loans; and
o The enterprise zone linkage.

INTRODUCTION

The National Council for Urban Economic Development (CUED) reported in June 1988 that the proportion of CDBG funds directed toward local economic development dropped from 13% in 1986 to 10% in FY 1987. This is considered a significant amount in terms of funding. Today, new regulations governing the CDBG program, along with the guidelines outlined in the Stokvis memo of June 1987, are creating hardship and confusion for city and state officials as well as businesspersons. Specifically, many administrators and beneficiaries of CDBG funds find it inordinately difficult to document eligibility of activities. Recipients must certify that the funds are used for projects that benefit low and moderate income families, aid in the prevention or elimination of slums or blight, or meet an urgent need. Also authorized is assistance to for-profit firms where the aid is deemed "necessary or appropriate" to carry out an economic development project. Grantees must determine the eligibility of projects according to regulations and maintain documentation of the determination.

CDBG is designed to benefit low and moderate income people. When the funds are used for economic development activities, this benefit generally takes the form of job creation and retention. Recipients must prove that 51 percent of the jobs created or retained through a project will be held by, or be available to, low and moderate income workers.

Loans to businesses for working capital and equipment are an effective economic development tool. Small businesses can be significant generators of new jobs. But the low-mod income requirements of the CDBG program tend to limit support to industries that have low wage scales and limited opportunities for skill and wage advancement. Some loan program administrators say that they only work with firms they know will meet the low-mod income requirements; for example, restaurants and cleaning services. In fact, Dayton, Ohio officials indicate that they use CDBG primarily for this purpose. They must leverage different resources for projects designed to have a broad impact on the economic base, such as marketing to attract high-tech firms. Efforts to upgrade and diversify the economy using CDBG are hampered by the forced focus on service industries with low-paying jobs.

PROVING ELIGIBILITY

Low-Mod Income Requirements Producing the necessary data to prove project eligibility is no small feat. Before the new regulations and the Stokvis memo were issued, some cities simply looked at the individual incomes of employees (or potential employees) to determine if they met the low-mod requirement. If the amount earned was equal to or less than the Section 8 lower income limit established by HUD, these individuals were considered as meeting the criteria. However, new rules specify that the employee's total family income must meet the low-mod requirement. HUD will accept either a written certification of family income and size or an agreement from the assisted business to accept referrals from public employment agencies with income restrictions equal to, or more stringent than, HUD criteria. Proving project eligibility also means documenting number of jobs created, the process used for "first consideration," the persons considered for available jobs, and who was hired.

Unfortunately, many small businesses do not have the resources to track and compile the data. Nor do they have employees who are necessarily willing to provide it. Under the regulations, recipients may submit certification signed by the employee that his or her family income is within the limits. But in at least one city, workers asked to provide the information gave the reply "none of your business." And legally, it may well be "none of their business." It is unclear whether these sorts of questions are invasions of privacy and possibly illegal under state civil rights laws; nor do we know for certain if an employer has the right to fire, or refuse to hire, persons who won't provide data on their financial status. The bottom line is, if you can't get the information, your project or business may be declared ineligible.

The Stokvis memo states clearly that low-paying jobs held by low income individuals don't automatically meet the low-mod benefit standard. But economic and community development officials know from experience that it is highly unlikely that low wage jobs will be held by members of high income families, particularly when the jobs in question are minimum wage.

Recipients of CDBG funds can also meet low-mod job requirements by documenting that at least 51% of the positions are made available to low and moderate income persons. This involves a written commitment from the business certifying availability and promising to provide training for any jobs requiring substantial additional education, experience, or training (defined in the Stokvis memo as greater than one year beyond high school). The memo also calls for analysis of hiring practices, including a firm's interviewing techniques and hires, to be sure that first consideration is given to low and moderate income people. Meeting each of these demands can easily constitute a hardship for the assisted (probably small) business.

Finally, eligibility can be achieved through a commitment to accept job referrals from public employment agencies. But this, too, is problematic. The percentage of jobs filled through referrals is typically low, so if a company eventually turns to hiring on its own, HUD steps in to require that additional income data be collected from each non-agency hire. This happened in Portland, Oregon, which has since developed its own job referral service. And in Miami, PIC programs only offer help to the very poor (individual income $5,600; family of four $12,500), so a large number of CDBG eligible persons cannot be served by these programs.

Another unanswered question concerns whether a job qualifies as benefiting a low or moderate income person if the job itself causes the person's income to rise above low-mod. The regulations say that "whether they continue to meet that definition or not, the benefit to the low and moderate income person is clear." But local officials cite examples of HUD field staff who maintain, on the basis of the Stokvis memo, that a job meets the criteria only when it is held by a low or moderate income person. This disqualifies jobs that raise a worker's income above low-mod.

Activities that benefit residents in an area where at least 51% of the population has low or moderate income are also eligible for block grant assistance; yet it is hard to document the service area of an assisted business. In Miami, the city planned to help five abutting businesses improve their storefronts in a targeted business corridor. HUD approved only four of the five; the fifth was declared ineligible because it was a wholesale business that HUD decided didn't provide sufficient benefits to low-mod residents. The city stepped in to qualify the business under the low-mod job benefits criteria, but if it had been unable to do so, an incomplete facade improvement project would have resulted. The business may have chosen to relocate. The project was also delayed for 18 months by HUD field staff because of Davis-Bacon concerns. Basically, it seemed that field staff focused its attention on whether the project met a series of strict and confusing regulations rather than whether it made sense and complemented the original statute.

ADDITIONAL ELIGIBILITY CONDITIONS

Necessary or Appropriate Regulations require that a "necessary or appropriate" determination be made whenever CDBG assistance is given to a for-profit entity for an economic development project. Documentation to HUD must include a financial analysis of the business' need for funding and show that the amount is not excessive. Public benefits to be derived from the project have to be demonstrated as well. Not surprisingly, this is a "gray area" in the regulations; it complicates the decision-making process. Economic and community development professionals say that it is harder to determine the subsidy needed for a business versus a housing project. Projects costs and revenues are not as easily identified, especially for larger companies or manufacturing firms. Yet HUD officials require that capital needs and financing gaps related to business expansion be justified according to rigid HUD formulas. For example, a 5 to 10 year pro forma is generally demanded for a proposed project. This is inconsistent with commercial lending guidelines, which typically do not require pro formas of more than 3 to 5 years. Figures beyond this period are considered to be guesswork. Also, CDBG loan regulations are designed to provide the minimum amount of assistance necessary to make the project financially feasible, with the minimum rate of return to the borrower. In contrast, banks are not concerned with the borrower's rate of return, only with the borrower's ability to repay the loan. Finally, local officials have expressed concern that HUD auditors do not have the necessary background in business or banking to evaluate the assisted projects.

Davis-Bacon Construction and rehab projects are eligible economic development activities. But prevailing wage requirements set by Davis-Bacon discourage private participation in these projects and result in significant administrative costs to the public. Davis-Bacon requirements were estimated to add between 10 and 20 percent to the cost of construction and rehab projects in Portland. In rehab projects especially, the subsidy provided often does not justify the additional cost. Dayton, Ohio officials (and those from other cities as well) say that they avoid doing construction projects with CDBG funds. Cleveland uses CDBG primarily for real estate projects, and officials there also say that Davis-Bacon is their biggest headache. The requirements make smaller non-residential neighborhood projects virtually impossible. For example, one developer was planning to rehabilitate a vacant bank building on the outskirts of a deteriorating neighborhood. He applied for and received a UDAG, but after analyzing his numbers according to

Davis-Bacon wage rules, he concluded that it would be less expensive to use conventional financing. This meant that the project would be prolonged and perhaps even die because of the need to raise additional capital. Loss of a UDAG means, too, that the city will not have the same control over the project design. Essentially, though the Labor/HUD compromise on Davis-Bacon last summer has provided extra flexibility, it is still short of what's needed to make CDBG (or UDAG) work. Professionals that use CDBG for development projects suggest that a limit based on project size ($1 million, for example) should be established, under which Davis-Bacon would not apply.

THE COMMUNITY BURDEN

Administrative Communities that use CDBG are frustrated that they must spend far more staff time verifying and monitoring employees' incomes at assisted businesses rather than developing and implementing programs. The Portland Development Commission estimates that for every dollar loaned through CDBG, it spends 50 cents to administer the loan, going back year after year to a business to get more information to fulfill additional HUD requests. This administrative burden, in addition to other fiscal restraints and priorities, has caused Portland to reduce its loan program from $900,000 to $250,000 this year; more attention will be focused on neighborhood revitalization instead.

Limited Focus The HUD guidelines limit economic development activities to those that can be linked to a majority of low and moderate income persons. In many cities this ultimately means loan programs and nothing else. It is harder to prove the link for economic development functions performed through business retention specialists, industrial property inventories, and technical assistance. Marketing activities, needed to improve a program's effectiveness and attract business to the community, are also restricted by the documentation requirements. For instance, a $50,000 marketing brochure and campaign developed by the city of Miami to encourage investment in low-mod neighborhoods was challenged by HUD monitors because the brochure discussed general facets of the city as well.

Miami uses its CDBG program to fund a number of intermediary organizations that operate economic development programs. These community-based organizations (CBOs) often use the funds to support administrative activities, as they can find no other resources to do so. HUD is challenging this use, arguing that assistance for CBO operational expenses falls under the 20% administrative cap. The department has, in fact, begun questioning the eligibility of many of Miami's economic development programs. The city has found that virtually the only activities it can perform without being challenged are infrastructure projects such as facade improvements. HUD field staff is making determinations, based on the June 1987 Stokvis memo, that money paid to consultants for technical assistance in capacity building is an administrative expense that is subject to the 20% cap. The city and HUD disagree on whether technical assistance qualifies as a direct program expense. While there is no mention of this in the Stokvis memo, the regulations do list technical assistance as an authorized economic development activity. HUD staff seems unaware of this.

Portland has tried to use its CDBG funds for recruitment efforts. The city offers site selection services, location assistance, technical assistance and employment and training referrals to businesses considering locating in Portland. The city has to document where the funds are going now; it cannot highlight the recruitment strategy's long-term benefits in terms of job opportunities and tax revenues. This narrow perspective makes it difficult to use CDBG money to attract a high-tech firm that would generate 2,500 jobs over five years, because the jobs available to low and moderate income persons would surely be less than 51%. However, this ignores the fact that such a firm might provide low-skilled workers an opportunity to move into higher paying positions with training. Portland develops employment agreements with new and incoming companies and requires placement of 51% low-mod persons. The city also requires extensive record-keeping.

THE PRIVATE BURDEN

Disincentives to Participation The cumbersome reporting requirements of the low-mod income guidelines discourage businesses as well as cities. The Detroit Economic Growth Corporation (DEGC), for example, operates business attraction and retention programs, offering CDBG loans as an incentive for firms considering Detroit. However, a businessperson who receives this type of help from DEGC is also subject to the onerous regulations, and it is not unusual for the business to simply go elsewhere to avoid the hassle.

Other activities not directly linked to the low-mod job benefit standard are affected, too. In Cranston, Rhode Island, the city's economic development office provides assistance for marketing, technical assistance and job training linkage programs. However, businesses receiving this assistance are required to document the low-mod benefit. A survey of the recipients showed a very negative response to the reporting requirements. The city was then unable to provide the necessary documentation to support these activities and lost $95,000 in CDBG funds. This is especially unfortunate considering that the funds had been used to support an office of economic development that had created 6,600 employment opportunities.

Businesses that consider staying in or moving to distressed inner-city areas are taking a considerable risk. Cities need to provide some incentive to those firms to invest in these areas and hire local workers. However, the CDBG regs make it difficult for cities to offer such an incentive, even a small show of good will. If a firm is eligible for private financing, then it cannot get CDBG money -- and this private loan is inevitably used to move elsewhere, exactly what the city wishes to avoid. Moreover, the CDBG requirements provide a disincentive to that business to participate in the program.

CREATING A SECONDARY MARKET FOR CD LOANS

Local governments have the option (and should be encouraged) to sell their loan portfolios to generate revenue for economic development activities. Securitization is a potential source of fresh capital that can be used to make additional loans once the proper mechanisms are in place. The major constraint traditionally has been that there is no reasonable vehicle for locating investors willing and able to purchase this type of security. And state and local officials are concerned about maintaining their responsibilities to initial borrowers and meeting the requirements of the loan (such as the CDBG low-mod job benefits). There are ways to deal with this, though: the city can continue to service and monitor the loans and guarantee that it will buy back from the portfolio any loans that go into default. Another option, when the rate of return on the loans does not generate enough revenue to justify the sale, is to use the loans for collateral for other borrowing. A final concern for CDBG loans is how the revenue generated from the portfolio sale is treated in terms of program and grant administration. HUD regs consider the revenue as program income that can be used for CDBG-eligible activity. However, program income must be used before the city can draw down on current CDBG funds.

CDBG REGULATIONS WORK AGAINST THE PROGRAM'S STATED GOALS

CDBG recipients are concerned that record-keeping and documentation requirements are effectively determining what types of assistance are available. This is not the intent of the statute. HUD field representatives apparently think in strictly black and white terms -- if the recipient cannot provide the records to meet the regulatory standards, then the activity is ineligible, period. This standard excludes many legitimate economic development activities. For example, Detroit can no longer fund the DEGC to carry out business attraction programs because DEGC cannot prove low-mod benefits to HUD's satisfaction -- even though Detroit's population is 60% low and moderate income. Currently, the city uses CDBG only as a stopgap measure on certain DEGC programs. It would appear that without changing the regulations, HUD could allow the business attraction and other activities if it would agree that new hires simply had to be city residents (since the entire city would qualify as a CDBG target area). In Philadelphia, HUD has charged two city economic development agencies with failing to report regularly on the number of jobs created, and failing to meet hiring goals promised when they applied for low-interest loans. Because of the dispute between HUD and the agencies, the city has frozen about $1 million in CDBG funds. The agencies fear that dozens of companies counting on the financial assistance will be hurt unless HUD relaxes its regulations as well as the penalties it plans to exact from the agencies.

Cities have been forced to discontinue numerous economic development activities; for example, business retention efforts because of the difficulty of documenting the low-mod benefit standard for jobs retained. Cities that continue to operate CDBG loan programs report decreased lending activity due to confusion over regulations and cumbersome reporting requirements. In Miami Beach, the Interim Finance Program, which is a "CD Float," has experienced a considerable drop in activity thanks to the added criterion for a "necessary and appropriate" determination. In some cases, businesses that would have been assisted seek other sources of financing; in other cases, the projects die altogether. At any rate, the regulations are viewed as a deterrent to development; they diminish the desire of private businesses to seek public support to expand and prosper.

It's time to consider the fact that the economic situation in many cities has changed since CDBG regulations governing economic development were first written. Unemployment has fallen and the labor shortage is the major issue for many firms seeking to grow. Job training designed to get people back into the workforce is a key economic development concern. Yet cities that rely on CDBG funds for economic development are prevented from using their resources to develop appropriate programs. The guidelines are just too inflexible. Secretary Kemp has said he believes strongly in CDBG as an economic development tool. However, the current rules discourage entitlement communities from using innovative methods to leverage additional resources, and communities whose economic development activities are supported chiefly by CDBG are limited in what they can do to create opportunities.

LINK TO ENTERPRISE ZONES

Secretary Jack Kemp has targeted enterprise zones as a means of job creation for low and moderate income individuals. But the current CDBG regulations may make it fairly difficult to target business assistance to zones. For CDBG to be used to help a business in an enterprise zone, that assistance would still need to meet one of the national objectives as well as the necessary and appropriate determination. As stated, most cities have found that these criteria are met only by assisting small firms with low wage scales. Assistance to larger, established firms is often not possible when the "necessary" clause is interpreted as a "but for" determination.

This inability to use CDBG to help larger firms is particularly significant when enterprise zones are the focus of economic development activities. Job creation in zones has been shown to be generated by the manufacturing sector. According to a Pennsylvania State University study, manufacturing accounts for 73% of all net new jobs created in enterprise zones. These firms clearly require financial incentives to locate in disadvantaged areas, but CDBG does not, at present, provide that incentive.

RESPONSE TO CUED'S "GLAUDE MEMO"

The National Council for Urban Economic Development has received quite a positive response to the CDBG memorandum it produced for Stephen Glaude, Deputy Assistant Secretary for Program Management at HUD. The memo outlined in greater detail the issues discussed in this testimony. The executive director of Gulfport, Mississippi's Community Development Commission remarked that answers to the CDBG difficulties had begun to seem so remote she was no longer "sure of the problems anymore." She was relieved that CUED had voiced the concerns of so many economic development practitioners and local officials.

Coalition
for Low-Income Community Development

October 3, 1989

Ms. Eileen Gallagher
Senate Subcommittee on Housing and Urban Affairs
535 Dirksen Senate Office
Washington, D.C. 20510

Dear Ms. Galigaher:

I have enclosed the Coalition for Low-Income Community Development's (CL-ICD) formal written testimony for submission to the record for the September 8th Roundtable hearing on the Reauthorization of Community and Urban Development Programs. Thank you for allowing us to particpate in the Roundtable. We found the format very effective and recommend its use over the more traditional hearing structure.

During the Roundtable discussion, one of our witnesses, Preddy Ray, stated that some Congresspeople felt that because the program was not highly targeted it could not be as easily defended during the budget process. Jeffrey Swaine from Rochester asked Mr. Ray to state the name of a Congressman who felt that way, and Mr. Ray said we would provide that name to you in writing. For the record, we would like you to know that Congressman Bill Gray had such a discussion with CL-ICD's co-chair, Belinda Mayo, from Philadelphia, Pennsylvania.

If you have any other questions about our testimony or our particiaption in the Roundtable, do not hesitate to call me.

Sincerely,

Karen Stokes

Karen Stokes
Executive Director

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TESTIMONY OF THE
COALITION FOR LOW-INCOME COMMUNITY DEVELOPMENT

Roundtable Hearing on the Reauthorization or Community and Urban Development Programs

September 8, 1989

Mr. Chairman, Members of the Committee, we greatly appreciate the opportunity to share the views of the Coalition for Low-Income Community Development (CL-ICD) with you on the occasion of the 1989 reauthorization of the Community Development Block Grant Program (CDBG). We would also like to take this opportunity to thank Senator Cranston for his leadership on community development and for the initiation of this roundtable discussion format.

The Coalition for Low-Income Community Development (CL-ICD), is an active coalition of 700 grassroots and national organizations interested in CDBG and economic development issues. The Coalition was organized to preserve CDBG funding, as well as initiate and promote legislative and regulatory changes to ensure that low-income people benefit from the program.

In anticipation of the reauthorization process needed for CDBG in 1989, CL-ICD sought ideas from neighborhood groups and state coalitions around the country on how CDBG could be improved. In the fall of 1988, CL-ICD surveyed its membership about what policy priorities they wanted it to pursue and in January 1989, we held a meeting with representatives from both national and local organizations to formulate its public policy agenda.

In summary, CL-ICD's program recommendations are:

- CDBG should receive at least $5 billion dollars in funding;

- increasing the targeting of CDBG funds from 60% to 75% to low and moderate income persons and adding a second-tier targeting requirement of 40% to low income people;

- proposing the requirement of an economic development strategy plan which describes the needs of low/moderate income persons and how grant activities will meet those needs and target employment training and jobs while minimizing displacement of existing businesses and jobs;

- including a requirement that projects receiving CDBG funding comply with Federal Wage and Hour, OSHA, and Worker's Compensation standards;

- ensuring that for the Entitlement Program, 25% of all program activities contracted out by local governments must be carried out by community-based organizations;

- advocating that non-profits should be able to apply directly to the State for CDBG funds in the States and Small Cities Program if the local government does not apply. All non-profits applications would need local government sign-off;

- proposing stronger legislative language to protect low-income people against indirect displacement caused by CDBG funded projects.

Before we discuss our program recommendations in detail, we would like to elaborate on the importance of the CDBG program to low-income communities. This past August 22, we celebrated the 15th anniversary of the CDBG program. There is no doubt that the CDBG program has become the most important single resource for low-income community organizations. Community development corporations seeking financing for low-income projects, community -based service providers, and neighborhood groups advocating for improved housing, economic development, and better services all find the Community Development Program central to their needs.

The reasons for this are simple: other programs supporting low-income housing and economic development have been cut heavily, and CDBG is a $3 billion dollar resource, controlled at the local level, flexible and yet targeted to benefit lower-income people. Although it has been cut by almost one-quarter in recent years, the Community Development Program has come to dwarf all other sources of funds for housing rehabilitation and conservation, job creation and training, commercial and industrial development, and neighborhood revitalization, as other programs have been cut far more sharply or totally eliminated.

CDBG's significance is especially great for community organizations. Because 60% of the CD funds are supposed to be spent in ways which benefit low and moderate income people, and because the CD program stresses housing, social services, and economic development projects, it is a particularly vital source of support for neighborhood groups which operate these kinds of programs.

The CDBG Program is especially vital as a source of loans and grants for housing rehabilitation, commerical strip revitalization, and basic services for low-income communities. For many community-based service providers and development corporations which operate their own neighborhood improvement projects, CDBG is also a vital source of funding for central staff.

This importance was recently underscored by a study which the Local Initiatives Support Corporation (LISC) conducted of projects which it supported with loans, grants, and technical assistance. Fully 62% of these projects depended directly upon the CDBG program for support. Furthermore, many of the community development corporations surveyed had received CD funds for other projects or for central administrative and staff costs, bringing the overall percentage of LISC-supported groups which depended upon CD funding to well over 80%.

Problems with the program

We approach this 15th anniversary of the CDBG program with some concern and skepticism about the efficacy of the program, however. It is somewhat ironic that the CDBG program has become so crucial to low-income community groups. Neighborhood organizations have often been the most vocal critics of the program, monitoring how it is being implemented at the local level, pointing out illegalities and questionable priorities, and challenging waste and ineffective programs. Although the funds are essential to many low-income organizations and communities, many more eligible and needy low-income neighborhoods are not benefiting from these scarce federal dollars because of the way the program is administered locally.

Since CDBG is administered as a block grant program, there are tremendous differences from state to state, county to county, and city to city, in how effectively the program is administered. One of the strengths of the program, its diversity, is also a problem since CDBG's success in meeting the national objectives of the program is also quite different from jurisdiction to jurisdiction.

As the CD program itself has suffered cuts and other programs have been eliminated, the struggle over how the remaining money is spent has intensified. Local and state governments have been tempted to divert CD funds away from low-income neighborhoods to cover general government functions historically supported with local revenues and General Revenue Sharing. In addition, although the program mandates that 60% of CDBG funds are targeted to low and moderate income people, there is no assurance that low -income communities are given their fair share of the funding.

There has always been tension between low-income neighborhood groups and local and state officials on how CDBG funds should be spent. Low-income community-based groups naturally are committed to making sure that CD funds are spent in the neighborhoods which have the most serious housing, economic development, and service needs -- their neighborhoods. Low-income groups stress that the law requires that the "principal beneficiaries" of CD spending be low and moderate income people.

Local and state officials, on the other hand, understandably have their own priorities, which often differ from those of low-income people. Public officials tend to be far more interested in using CDBG funds to cover government's administrative expenses, basic public services, downtown development projects, and public works than in using them for low-income housing and other low-income neighborhood priorities.

We recently presented our program recommendations to a number of organizations which also have an interest in CDBG. You will hear from many of them today in this roundtable discussion. CL-ICD has been criticized for recommending "sweeping changes" to CDBG and for criticizing a program which runs well and is flexible enough to meet the needs of each very diverse community in our country.

We do not take issue with the need for CDBG to be a flexible, locally-oriented and accountable program. We also believe that flexibility and diversity are critical to the success of the program. We do not believe, however, that our program recommendations take away from the flexibility of the CDBG program. Our recommendations merely provide tools and directions to ensure that the important national objectives which were the inspiration for the original legislation are met.

The principal beneficiaries of the program are supposed to be low and moderate income people. Our Coalition naturally places a greater emphasis on the needs of low income people. We do that for a number of reasons - we represent them, and more importantly, we believe that it is appropriate, given the scarcity of federal dollars and the urgency of their problems, to ensure that the needs of low-income communities are guaranteed through national legislation.

Since 1986, CL-ICD has led the struggle for increased priority of funding and has assisted low-income organizations and communities on CDBG issues. While arguing for full funding of the CD program, CL-ICD has criticized a number of major weaknesses in the program, and Congress has taken these concerns seriously. In particular, in 1987 Congress amended the CDBG legislation in three ways, each benefiting low-income neighborhoods and the CDCs and community organizations which serve them.

First, Congress agreed to increase the targeting of funds allocated to projects which benefit low and moderate income people from 51% to 60%. Second, Congress strengthened citizen participation standards for the CD program. While not a significant change for many major cities, this was a breakthrough for community groups and citizens in smaller jurisdictions and rural areas, where access to information and opportunities to participate in decision-making have been lacking. Third, the bill included new anti-displacement requirements.

CL-ICD focussed on these areas as needing national reform. It documented problems with the program, stressed the need for more funding to address the problems of homelessness, inadequate housing, unemployment, and unmet social service needs throughout the country. Reminded of these needs, Congress chose to act. We ask you to listen to our recommendations today, think about what we are suggesting, and as you did in 1987, we urge you to choose to once again lead Congress in improving this much needed program for our nation's low-income communities.

CL-ICD's program recommendations

I. FUNDING

We propose that the following changes should be linked to a two year reauthorization of the program for $5 billion dollars annually, with full appropriations and without any deferrals or rescissions. This level of appropriation is actually equal to funding CDBG at 1981 levels, adjusted for inflation. The current funding level of $3 billion, is woefully inadequate since the number of eligible communities has increased substantially since 1975, while CDBG funding has decreased during the same period of time. For example, there are 211 more eligible CDBG entitlement communities since 1979 and the funding of this part of the program has decreased by $779 million dollars.

II. FEDERAL/LOCAL ASPECTS OF THE PROGRAM

INCREASE THE ROLE OF NON-PROFITS IN COMMUNITY DEVELOPMENT

The emergence of non-profit community-based housing and development organizations is probably one of the greatest changes which has occurred in the development field since the CD legislation was first enacted in 1974. The increase in the number of successful Community Development Corporations (CDCs) is the most obvious example of how non-profits are changing how community development can and should be done in this country. CDCs are non-profit organizations, are accountable to the communities in which they operate, and are development corporations.

According to recent research by the National Congress for Community and Economic Development (NCCED), between 1,500 and 2,000 CDCs are now operating that have completed at least one development project. Rehabilitation and construction of low-income housing are the primary activity of most CDCs. The 631 CDCs responding to NCCED's survey report the production of 125,000 housing units. CDCs also develop commercial and industrial facilities, provide social services, such as job placement, and advocate on behalf of their constituents. The ultimate misssion for many CDCs is to reduce poverty, stabilize distressed or declining neighborhoods, and gain economic power for their communities. Housing low- and moderate- income people is thus not just an end in its own right, but also a tool for achieving this broader mission.

The first CDCs drew attention in the late 1960s and 1970s as attractive development vehicles because of their commitment and sensitivity to community needs in selecting, structuring and implementing projects. CDCs and other community-based non-profits enable low-income community residents to take direct control over whether and how development takes place in their neighborhoods. Absent CDC involvement, many low-income neighborhoods saw no development at all. CDCs enable low-income community residents to define the scope, design, and location of proposed ventures, as well as to participate in the political process through which many development decisions are made.

The ability of non-profits to work collaboratively with a wide range of public and private sector institutions has grown dramatically. CDCs and similar community-based groups have been earning their place at the negotiating table with mayors, bankers, and profit-motivated developers by contributing tenacity, a respected voice for their neighborhoods, and growing technical sophistication - critical ingredients in rebuilding communities.

The increase in technical and financial support available to CDCs has grown substantially, enabling more CDCs to get started and undertake more complex projects. The advent of non-profit "intermediaries" such as LISC, the Enterprise Foundation, and the Neighborhood Reinvestment Corporation, has also helped to expand CDC and other community organizations resources.

Our recommendation for the increased involvement of non-profits is not based on our desire to simply target greater funding to the groups who are part of CL-ICD. We believe that successful CD is that community development which is developed, accountable, and completed by the actual community. An integral part of community development is empowering the community to improve itself, to be a full partner in its own development. The process does not as easily or as successfully occur when city government and for-profit developers come in to develop a neighborhood.

CDCs and other community-based organizations have a knowledge of local housing needs, markets and opportunities, as well as an ability to draft flexible and effective programs that respond to these local circumstances. And most importantly, they have a commitment to serving low-income households on a long-term basis. They are willing to undertake projects that profit motivated developers consider too small, too risky, insufficiently profitable, and located in neighborhoods that are too distressed. Non-profit community-based organizations have the political and technical skills to assemble multiple public, private, and charitable resources to make projects feasible and are able to marshall community support.

CL-ICD is proposing two recommendations which would increase the role of non-profits in community development.

1. Non-profits should be able to apply to the State for CDBG funds in the States and Small Cities Program in those jurisdictions where the local government is either unwilling or unable to apply to the State for funds. The non-profit application should be approved and signed-off by the State.

We believe that non-profits in the States and Small Cities Program should have the same opportunities as non-profits in the Entitlement Program to apply for funding. This change would ensure that rural non-profits with good ideas and track records, would have an opportunity to at least apply to their State for CDBG funding.

2. We are recommending that, in the Entitlement Program, for all contracted out program activities, HUD should require that local governments give maximum feasible priority to funding programs operated by non-profit, community-based organizations. We further recommend that within three years after this recommendation becomes law, not less than 25% of the funds provided by the recipient for economic development, housing, and services projects are allocated to neighborhood or community-based non-profit organizations.

We have attached to this testimony, draft language for legislation for both of these recommendations.

III. INCREASED TARGETING

CL-ICD is proposing three changes in how the CDBG program is targeted.

1. PROPORTIONATE ACCOUNTING - Modifying the method for calculating benefit to low/moderate income persons

CDBG funds could be more effectively targeted to low-income people through proportionate counting. The current situation permits the jurisdiction to count 100% of an activity's money as benefiting lower income people, even if only 51% of the activity's users are actually lower income people. We propose that if only 51% lower income, then a locality should only count 51% (or whatever the percent happens to be - 66% or 72%) of its spending on an activity toward the minimum required to count towards low and moderate income program benefit. Proportionate accounting should apply to areawide benefit activities, job benefit activities, and limited clientele activities. It already applies to housing activities.

An example will help make this idea clearer. An economic development project getting $1,000,000 in CDBG money will create 100 jobs. Currently 51% of the jobs must be available to lower income people if this project is to count toward the local government's 60% Benefit Requirement. If 51 of those 100 jobs really do go to lower income people, then the project will qualify as one that benefits lower income people. However, instead of counting $510,000 (51% of the CDBG subsidy) toward the 60% Benefit Requirement, HUD's rule allows all $1,000,000 (100% of the CDBG subsidy) to be counted, even though far less than 100% of the jobs were available to lower income people.

2. INCREASED TARGETING OF CDBG FUNDS FROM 60% TO 75% TO LOW AND MODERATE INCOME PEOPLE AND REQUIRING THAT 40% OF THIS EARMARKED MONEY MUST SPECIFICALLY BE TARGETED TO LOW-INCOME PEOPLE (below 50% median income);

We believe increased targeting of the program is important for two reasons:

a) since the needs of lower income people are extremely urgent, with worsening housing, homelessness, persistent unemployment, and inadequate services, we believe requiring that at least 75% of these funds benefit low and moderate income people is only appropriate;

b) an increased targeting requirement will better protect the program during the budget process when higher priority is given to progams which serve poor people.

Although the CDBG program gives preference to projects which benefit lower income people, this targeting is only partial. Evaluations of CDBG spending have repeatedly shown that -- while the program supports many essential housing, economic development, and service activities -- much of the money is spent on projects which are of a low national priority.
For example, in many jurisdictions, substantial portions of the funds are used for administrative staff, including people who have little, if anything to do with local community development. Some jurisdictions currently use over 25% of the funds to cover government staff salaries and overhead, and seem tempted to use increasing amounts of the CDBG funding to cover activities previosuly funded under General Revenue Sharing.

Furthermore there are many examples of funds being used for downtown beautification and parking lots, or curbs and gutters in middle class neighborhoods, rather than vital projects to address homelessness, abandonment, long-term unemployment, and other desperate needs.

We were pleased to see that in 1987 Congress increased the targeting of funds allocated to projects which benefit low and moderate income people from 51% to 60%. Although this was an important step, we believe that a 75% targeting level more appropriately reflects the national objective which mandates that the program principally serves low and moderate income people. We do not believe that a 75% targeting requirement is either unreasonable or unjustified - especially in light of the increased pressure on scarce federal funds to be carefully spent on the neediest communities and programs.

In addition, we are recommending that at least 40% of this 75% must be targeted to people 50% and below the median income in the SMSA. We believe that such a 40% designation is a minimal amount, and a figure which every jurisdiction shoud be able to attain if they are meeting the spirit of the CDBG law. These targeted amounts would mean that 45% of total CDBG funds would go to low and moderate income people (up to 80% of the median), 30% would be targeted to low income people (50% and below the median) and the last 25% is not targeted at all. We believe that these national targets are appropriate guidelines which local governments can and should meet. They do not threaten the flexibility of the block grant program.

Concerns about the CDBG program have increased because of the unpredictability of the federal budget process. Under this process, the CD program has not been considered to be a "high priority, low-income" program protected against budget cuts. Funding levels, in terms of real dollars, have been reduced dramatically. The funding of CDBG is directly related to the Coalition's interest in increased targeting of the program. If we cannot easily increase the dollars for the program, we are at least trying to increase the amount of funds targeted specifically to low-income communities. CL-ICD also believes that a "better targeted" program means a "better protected from budget cuts" program.

As the program is currently structured, few legislators in Congress see the CDBG program as one which benefits the "truly needy" and therefore are not committed to saving this program. Many see it as imperfectly targeted, trying to be all things to all people, and being almost as difficult to defend in a time of federal austerity as General Revenue Sharing. To survive, the CDBG program must gain much stronger support in the budget process. This can best be done by making the program far more effective in serving the strong national purpose of meeting these most critical needs and improving housing, job, and business opportunities for low and moderate income people.

With tighter targeting and other legislative changes, CDBG could be an exceptional program. With modifications, it could combine the best aspects of decentralized administration and national standards and purpose, and it could spur the kinds of self-help and neighborhood revitalization, and closer scrutiny of economic development plans to make sure that they represent a sound investment of scarce resources.

IV. STRENGTHENING ANTI-DISPLACEMENT PROVISIONS

The impact of the 1987 antidisplacement provisions cannot be measured yet because, as HUD wrote the regulations, the provisions will not take effect in many jurisdictions until October 1, 1989. However, CDBG-induced displacement is very real, as powerfully demonstrated last year by the testimony regarding 29 projects at a House subcommittee hearing. Examples of displacement, despite the 1987 provisions, continue to emerge from locales such as Cocoa, Florida and Grand Rapids, Michigan.

At last year's House hearing, a few representatives of local government warned that the antidisplacement provisions would discourage economic development and housing-renovation. The Coalition recognizes, and in 1987 the Congress did too, that in far too many instances the costs of development are not internalized to the subsidized project. Rather, the development costs are usually externalized; so that low-income people pay for the cost of redevelopment for upper-income people. Low-income people's cost comes in the form of paying over 50% of their income for shelter, doubling up with relatives, enduring increasingly substandard replacement housing, or actual homelessness. The intent of the antidisplacement provisions is to make it too expensive to undertake development that increases homelessness.

Redevelopment intended to benefit lower-income people can be accomplished without undue relocation or expense. Staggared and well-planned redevelopmnet can avoid displacement, and can use CDBG funds to meet the costs of temporary relocation. Even redevelopment financed by CDBG for upper-income people can be accomplished. Testimony at last year's hearing showed how the developers of Brooklyn's Metrotech project found the money to both compensate displaced households and replace lost units on a one-for-one basis.

Indirect (off-site) displacement was the subject of testimony from six locales last year. CDBG subsidies do lead to off-site displacment. The work of Professor Elliot Sclar and of Maria Simpson is not only demonstrating the impact of off-site displacment, it also offers an easy, workable model for forecasting it. Using data and methods already utilized by the real estate industry, Professor Sclar and Peter Marcuse provided the House with a mechanism to assess the possible off-site displacement impact of a development project. Their model relys on information readily available and in use by developers,and it resembles the now familiar process of conducting an environmental impact assessment.

We propose changes to accomplish three objectives: 1) correct the law in response to HUD's interim regulations which violate the spirit, and in some instances, the letter of the law; 2) close loopholes in the law; and 3) make off-site (indirect) displacement subject to the law.

To accomplish these objectives we are suggesting the changes outlined below:

1. Prevent the use of Section 8 for relocation compensation or for meeting the one-for one housing unit replacement obligation. Use of Section 8 merely bumps other low-income people

from waiting lists, and it does not preserve the stock of affordable housing.

2. Clarify that CDBG-assisted code enforecement, public works, and planning can lead to direct displacement. A set of effects and conditions are proposed to help determine whether the anti-displacement provisions should be engaged.

3. Require affordable replacement dwellings to be placed on the market prior to the loss of existing affordable units through the use of CDBG. HUD's interim regulations allow for a three year gap.

4. Increase from five years to 15 years, the time displaced households must be ensured that their shelter costs will not exceed 30%.

5. Increase from 10 years to 20 years, the time replacement housing units must remain affordable.

6. Define "affordable housing" to low and moderate income households in a manner that will make replacement housing truly affordable to lower income people. HUD's regulations currently define affordable as FMR market rates.

7. Require replacement housing units to be available in the same or nearby community and that people displaced should be able to relocate in their own neighborhood.

8. Provide compensation to people displaced one year before CDBG money is sought for a project. For example, compensation should be provided to tenants forced from their apartments by landlords anticipating CDBG housing rehab money.

9. Prevent the displacement of low-income people by moderate income people.

10. Make UDAG "repayment" subject to the antidisplacement provisions.

V. HOP AND THE BLOCK GRANT

HOP funds should not limit the flexibility of CDBG. That is, in communities where lower-income people give highest priority to housing that is affordable to low-income people, CDBG money should be able to be used for housing purposes. No housing-related restrictions should be imposed on CDBG as a result of HOP's availability.

In addition, in order to ensure affordability to low-income people, deep subsidies are often necessary. Combinations of CDBG and HOP might often have to be substantial in order to make housing truly affordable. Therefore, any "protections" placed into law to preclude the provision of excessive federal subsidies to one development ought to be merely protections that prohibit double-dipping for projects that benefit middle and upper income individuals. "Protections" should not preclude affordability.

VI. ECONOMIC DEVELOPMENT

After two studies by the Office of the Inspector General, it was found that CDBG funds for economic development failed in many respects. The number of jobs created was short of the number promised. The number of jobs for lower-income people was even lower. To the extent jobs were created for lower-income people, they were often low-paying, part-time jobs. OIG stated in both studies, "clearly, the intent of CDBG is not to create low-paying jobs, but rather to create jobs for members of low-to-moderate income families. The low-to-moderate income status should be based on family income before any employment created through economic development loans."

In response to the OIG, HUD developed field memoranda in 1987, followed by regulations that were effective in Ocotber 1988. These regulations are commendable. They can minimize the monitoring and performance problems noted by the OIG's and other studies. HUD's regs have the potential to ensure that lower-income people actually benefit from CDBG funds used to subsidize for-profit ventures. The elements of HUD's regs ought to be incorporated into the law to further protect and serve lower-income people.

HUD's regs might, in fact, discourage some projects which either do not truly need scarce CDBG funds, or that would inadequately serve lower-income people. That consequence, however, would seem consistent with Congressional intent. More tightly targeting the CDBG program should have only an indirect impact on the use of this resource for economic development. Targeting applies to a jurisdiction's aggregate spending. Therefore, with 75/40% targeting, each economic development project need not fill 75% of its new jobs slots with lower income people.

Rather than a decline, HUD reports an increase in the amount of CDBG funds dedicated to economic development. For entitlement jurisdictions, HUD reports that in FY 1988, $323 million of CDBG (13%) was planned for economic development. In FY 1987, $255 million (10%) was so planned. HUD reports that the States and Small Cities program's use of CDBG for economic development "expanded as a share of funding from FY 1982 to FY 1984 and remained roughly the same thereafter."

We recommend that all grantees of economic development funds be required to develop an economic development strategy plan which describes the needs of low and moderate income people, how their project will help meet those needs, and the nature and amount of long-term employment which will be created for low and moderate income people.

The strategy should also ensure that employment and training is targeted to people expected to reside in the jurisidiction of the grantee. Any economic development plan must minimize displacement of existing businesses and jobs and should include measures for documenting the extent to which project acitivities actually benefit low and moderate income people.

We also recommend including a requirement to ensure that projects receiving CDBG funding to support, create, or retain jobs, comply with Federal Wage and Hour standards, Occupational Safety and Health standards, and Worker's Compensation standards. We believe that workers paid with federal CDBG funds should be protected under these federal laws.

Conclusion

Once again we would like to thank you for the opportunity to share our experiences and views about the CDBG program with you today. The Community Development Block Grant is the most important source of federal funds for low-income community-based neighborhood groups and

CDCs. CDBG funding is virtually the only resource left for housing renovation, economic development projects, and neighborhood revitalization programs. It is clear that the 700 community groups which participate in CL-ICD value the CDBG program. We believe that the CDBG is a good program, but our proposed changes would make it an exceptional program.

On this fifteenth anniversary of the CDBG program, I suggest we all - Congress, locally elected officials, administrators of the program, non-profit organizations, as well as low-income communities - candidly assess this program. We cannot become complacent and sit back and say the program is adequate, the program works. Instead we should examine its strengths and weaknesses and resolve to further improve the program so we can likewise improve our nation's neighborhoods.

We ask you that you carefully consider the recommendations we have brought to you today and we urge you to take the lead in Congress to improve this much needed program so that it truly benefits our nation's low-income communities.

Thank you.

STATEMENT OF MARGARET KELLY, DEPUTY DIRECTOR THE NEIGHBORHOOD REINVESTMENT CORPORATION

Before the Senate Banking Subcommittee on Housing and Urban Affairs
September 8, 1989

Secretary Jack Kemp was recently quoted in "Insight" magazine as suggesting that HUD should no longer be focussed on building housing, but rather on building neighborhoods. Neighborhood Reinvestment's experience and comments regarding the effectiveness of the Community Development Block Grant program come from a strong neighborhood base which is reflective of our network of 218 resident-public-private partnerships in 136 cities across the country.

Much of our work is based on the assumption that if we can save, stabilize and strengthen neighborhoods we can successfully recreate communities where people feel proud and safe to live and raise their families, communities with quality affordable housing, communities which are economically and socially viable and self-reliant for the long term. The success of our efforts includes: 100,000 units of housing, 200 million dollars in low interest lending to "non-bankable residents, and six billion dollars reinvestment in neighborhoods that were generally written off. CDBG funds have been one of the most critical resource to the NHS Network's efforts and successes.

Over the last ten years we have focussed our resources and energies of difficult, marginal neighborhoods in markets as diverse as Stamford CT, Dallas TX, and Richland Center Wisconsin. Never before have we seen such wildly different conditions in our regional markets, and never before has there been such a critical need for a public resource with maximum flexibility to address neighborhood problems. The inherent strength of the CDBG program which must be protected is the tremendous degree of flexibility localities have nad in making use of this resource to most effectively meet the needs of their disadvantaged neighborhoods and their residents.

The CDBG program has provided a life line to many of these neighborhoods, and, in the process, has encouraged and enhanced the initiative of neighborhood tenants and homeowners in addressing their own local problems.

In the City of Lawrence, Massachusetts, one of the poorest cities in the State, the local NHS partnership and Community Development Department, with our help, have recently designed a comprehensive strategy to dramatically increase homeownership in the northern half of the City and aggressively confront and tackle the problems of drugs and drug related crimes which are endangering the neighborhood's safety and stability. The components of the strategy include a lender mortgage pool, a down payment assistance plan, a concentrated homebuyer counselling and follow-up program, tenant selection and training, and community organizing. CDBG funds of $275,000 over five-years available in a flexible fashion, will be the glue which cements the gaps between all of these other resources and makes this comprehensive 5-year strategy possible and viable.

No other resource has the breadth, the flexibility, or the potential to spearhead this kind of effort or to adjust to the requirements of the other key partners and funding sources. Without the CDBG program, this strategy would not have a chance of success and it is clear to all concerned that the situation in Lawrence would become far worse. Good tenants would simply move elsewhere, homeowners would sell, investors would become more careless, and ultimately, north Lawrence would be abandoned to drug dealers and to those with absolutely no other options. NHS, its resident leaders and the CD Department are stepping in aggressively, before it is too late, before the neighborhood economic mix has been lost, before everyone's equity in the neighborhood is dissipated and wasted. CDBG is the critical, flexible element in leveraging all of the other needed resources.

When you come from a neighborhood perspective you become fiercely protective of the aspects of CDBG funds which allow you to effectively address problems within the context of an entire neighborhood. Maintaining an economic mix in marginal neighborhoods is a tenuous but important endeavor. The ability to serve residents who earn up to 80% of median is essential to maintaining neighborhood stability and a healthy economic mix.

In many markets in the country even families at 80% of median are completely priced out of any ownership opportunities. Recent interviews with NHS Directors, Neighborhood Reinvestment senior staff and CD directors in Newark, Chicago, Boise, Atlanta, Oakland, Chelsea and Baltimore revealed that in each of these cities, families at 80% of median are priced out of all but the rental market and were, in terms of their housing options, as vulnerable as families making even less. The flexibility to serve the needs of an entire neighborhood has been crucial to the success of NHS. Transitional neighborhoods across this country need strategically placed resources designed to serve all of their residents if these neighborhoods are to be returned to health and soundness. While it is understandable, in a time of tight resources to target available dollars to the most needy as opposed to families and neighborhoods who are at the margin, in the case of CDBG dollars this decision would be terribly costly in the long run.

It is a bit like the well worn analogy of the two men standing on the river bank watching drowning victims float by. One man jumps in and hauls as many victims to shore as possible, saving only a few. The other goes upstream to find out who is pushing them in the first place. Much of the hardest, most effective work in our network, is in keeping people from falling - or being pushed - into the cracks. Those families at between 50% - 80% of median - the working poor in many instances - are extremely important to the fabric of our neighborhoods and the CDBG program is a critically important resource for them.

NATIONAL
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STATEMENT OF
THE HONORABLE D. MICHAEL STEWART
COMMISSIONER, SALT LAKE COUNTY, UTAH
AND
NACo FIRST VICE PRESIDENT

ON

COMMUNITY AND ECONOMIC DEVELOPMENT ISSUES
IN THE NATIONAL AFFORDABLE HOUSING ACT
S. 565

BEFORE THE
SENATE HOUSING AND URBAN AFFAIRS SUBCOMMITTEE

ON BEHALF OF
THE NATIONAL ASSOCIATION OF COUNTIES
WASHINGTON, D.C.

SEPTEMBER 8, 1989

The National Association of Counties (NACo)* applauds the Senate Housing and Urban Affairs Subcommittee for examining community and economic development issues in the context of refining the National Affordable Housing Act in which the centerpiece is the Housing Opportunity Partnership program. The vitally needed HOP program must be incorporated into a comprehensive community revitalization scheme.

While attention naturally has focused on creation of HOP, the framework of which county officials support, it is important not to overlook the critical role that the Community Development Block Grant program has played. CDBG and HOP should be companion programs because they both are essential tools in our efforts to provide decent living environments for all citizens.

County participation in CDBG has increased from 73 urban counties in fiscal 1975 to 122 direct entitlement counties in fiscal 1989. The expanded role of county governments in community and economic development mirrors the significant shift in the nation's population from rural areas and cities to the suburbs which generally constitute the jurisdiction of urban counties. This population shift provides county officials with challenges to provide public works, produce affordable housing for low and moderate income persons, ensure participation by all citizens in economic development, and develop an effective network of support services.

In addition to urban county participation in the CDBG program, 600 - 800 smaller counties with populations of less than 200,000 receive funds through state administered small cities programs.

Urban counties coordinate community and economic development initiatives among the 2,500 municipalities which participate through cooperation agreements in urban county CDBG programs. This intergovernmental approach helps to ensure that lower income persons throughout the county, including those in small pockets of poverty, are served. This helps to breakdown barriers between poorer and more affluent communities, thereby furthering the goal of spacial deconcentration of low and moderate income people throughout the county.

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*The National Association of Counties is the only national organization representing county government in the United States. Through its membership, urban, suburban and rural counties join together to build effective, responsive county government. The goals of the organization are to: improve county government; serve as the national spokesman for county government; act as a liaison between the nation's counties and other levels of government; and achieve public understanding of the role of counties in the federal system.

While NACo can site effective uses of CDBG, we also point out that the demand for these resouces far exceeds the program's authorized and appropriated funding levels. CDBG funds have been cut by 53 percent in constant dollars since fiscal 1980. These reductions have occurred despite an expansion in eligible activities, curtailment of federal housing programs, and an expansion in the number of entitlement communities. NACo urges an increase in the authorized and appropriated funding levels for CDBG to $4 billion.

The remainder of this statement will address specific community and economic development issues raised by the Senate Housing Subcommittee.

How is implementation of current law affecting displacement -- direct and indirect?

County officials find that compliance with two statutes and sets of regulations -- the Uniform Relocation Act and the relocation and replacement housing requirements that only apply to CDBG and UDAG funded projects -- is overly complex. NACo continues to urge that all federal displacement provisions be merged into the Uniform Relocation Act.

In response to stringent antidisplacement requirements that are contained in the Housing and Community Development Act of 1987, many counties are forced to avoid blighted projects that are likely to trigger this provision. For example, there is a disincentive to use CDBG funds for code enforcement even though the structure should be condemned for health and safety reasons. While counties readily acknowledge that affected tenants should receive relocation assistance, many counties simply do not have local resources to provide replacement housing and ensure that new units remain affordable for ten years. This concern is heightened by the decline in federal expenditures for rental subsidies and shortened terms of those commitments.

NACo urges the Subcommittee not to create a new category of indirect displacement. To do so would make local governments accountable for market forces over which they have no control.

Rent increases in most communities are sparked by private landlords who know they can extract rent hikes due to the scarcity of private rental units. Creating a class of indirect displacees, identifying potential claimants, and sorting out the proximate causes of rent increases could invite protracted and costly litigation. Making local governments accountable for indirect displacement would discourage public officials from undertaking efforts to preserve lower income units in transitional neighborhoods for fear they would be held liable for rent increases which actually are caused by market forces in the private sector.

Section 108 -- How could the program be made more useful? Is more leveraging, targetting possible?

Section 108 loan guarantees effectively have been used by many urban counties to implement large projects immediately rather than phasing in development or waiting until enough CDBG funds are available to undertake the project, which could adversely affect the timely drawdown of entitlement funds.

NACo supports legislation introduced by Rep. Tom Ridge to expand the Sec. 108 program. H.R. 2779, the "Community Enterprise Revitalization Act of 1989", would permit nonentitlement counties access to this development financing. It expands the repayment period from six years to 20 years, and increases the amount that a county could finance from three to five times its CDBG allotment. The bill also doubles the available credit in fiscal 1990 to $300 million, and then provides $500 million in fiscal 1991 and $700 million in fiscal 1992.

NACo does not support making housing construction an eligible activity under the Sec. 108 loan guarantee program. CDBG is not now, and should not become, a housing program. That is why HOP is needed.

What inappropriate impediments are in the way of economic development under the present CDBG structure?

Regulations promulgated by the Department of Housing and Urban Development are so restrictive and subject to misinterpretation that there is a growing reluctance to use CDBG for economic development. Even HUD area offices make inconsistent rulings as to whether a project conforms with the regulation's "necessary and appropriate" test.

HUD requires proof of a direct linkage between an economic development activity and the creation of low or moderate income jobs. In order to do so, businesses must verify that an employee's family income, not just the employee's income, falls within low or moderate income household guidelines. This entails considerable documentation that some businesses are unaccustomed and reluctant for privacy reasons to do.

Since HUD strictly ties economic development to job creation, counties cannot use CDBG to provide counseling services to small and minority businesses, because these enterprises may not actually create jobs until some time in the future.

Regardless of the percentage of low and moderate income families residing in an area, economic development projects do not qualify as area benefit activities. For example, counties have difficulty qualifying commercial revitalization in low and moderate income communities as an area benefit.

Counties often have difficulty substantiating that economic development assistance is both necessary and appropriate. For example, an out of state company contemplates closing a plant that is located in a low income community. A county may be able to show that the assistance is appropriate to retain jobs, but will have more difficulty proving that intervention is financially necessary. Unfortunately, clear and convincing evidence that assistance was necessary often does not materialize until a plant is on the verge of closing or has in fact closed.

What impediments have groups, states or localities found in using CDBG for community development? What refinements to law would they propose?

Some have advocated legislative changes to the CDBG program designed to (1) require broader and deeper targeting of funds, (2) utilize proportionate accounting in calculating low and moderate income benefit, (3) require a minimum set aside of funds for nonprofit organizations, (4) require a written economic development strategy, (5) add indirect displacement requirements, (6) expand citizen participation requirements, and (7) reduce allowable administrative costs.

As we understand them, these proposed changes are based generally on a perception that CDBG recipients do not serve the poor and that nonprofit entitles are better equipped to respond to community development needs. NACo takes strong issue with such assertions.

A survey conducted by the National Association for County Community and Economic Development of the 122 urban counties reveals unanimity that such changes are unncecessary, respond to isolated anecdotes, and would in many instances cripple urban county programs. The CDBG program was designed to meet the needs of low and moderate income persons and, in fact, serves this range of incomes.

CDBG gives localities the flexibility to design programs and projects that are tailored to local needs. Since the inception of the program, this flexibility has eroded as increasing layers of regulations have been added. Proposals to further target funds and place restrictions on how the program is administered would move CDBG closer to a categorical program -- the kind of programs CDBG replaced.

How would the housing component of CDBG continue to operate after the HOP is created?

As previously mentioned, there is an integral link between neighborhood revitalization and affordable housing. In response to the drastic curtailment of federal assistance for low income housing, counties have had to rely more heavily on CDBG for housing-related activities. Once the HOP program is authorized and funded, a greater portion of CDBG funds can be used for infrastructure and other public works that are essential for viable communities. CDBG also should remain a resource for housing rehabilitation and preservation while HOP funds primarily would be used to expand the supply of affordable housing.

Community Development Commission
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Deane Dana
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STATEMENT
OF
DAVID N. LUND
EXECUTIVE DIRECTOR
COMMUNITY DEVELOPMENT COMMISSION
COUNTY OF LOS ANGELES

ON

COMMUNITY AND ECONOMIC DEVELOPMENT ISSUES IN THE NATIONAL AFFORDABLE HOUSING ACT (S.565)

BEFORE THE
SENATE HOUSING AND URBAN AFFAIRS SUBCOMMITTEE

SEPTEMBER 8, 1989

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ISSUES FOR SENATE HOUSING SUBCOMMITTEE HEARING ON COMMUNITY AND ECONOMIC DEVELOPMENT

SEPTEMBER 8, 1989 AT 10:00 A.M.

ROOM SD 538, DIRKSEN SENATE OFFICE BUILDING

The Community Development Commission (CDC) County of Los Angeles functions in the unincorporated areas of the County; more than 50 cities have requested involvement in various CDC programs. As commissioners, the County Board of Supervisors sets policy for the agency.

The CDC is responsible for:

- directing the County's housing programs, including planning, finance, production, and conservation as well as administering the County's Section 8 and public housing projects;
- directing the Community Development Block Grant program, the largest Urban County program in the nation;
- financing community improvements such as resurfacing streets, rehabilitating homes and businesses, removing graffiti, and installing sewer and water lines;
- providing economic development and business revitalization services;
- redeveloping neighborhoods in target areas;
- providing comprehensive planning systems for housing and economic development; and
- providing revenue bonds, private financing, lease participations and loan agreements for the development of new rental and ownership housing as well as for economic development activities.

This statement addresses specific community and economic development issues raised by the Senate Housing Subcommittee.

MAJOR ISSUES

1. How is implementation of current law affecting displacement--direct or indirect?

   The Los Angeles Urban County expects to demolish approximately 65 low- and moderate-income dwelling units during the 1989-90 fiscal year. The County's policy has always been to minimize displacement; however, in some cases, especially where areas are seriously dilapidated, it cannot be avoided. Consequently, the current law regarding displacement has not significantly affected the amount of displacement that occurs in the Urban County Program. What the current displacement does do is add to the administrative and financial burden of an already over-burdened program.

   The tracking and monitoring requirements for the one-for-one replacement are burdensome due to the additional administrative costs, provisions for which have not been included in the legislation. Further, given that no additional funds have been provided for replacement housing, the ten-year restriction for replacement units can be difficult to achieve through the private sector. Each development package caries its own restrictions and if public funding is not involved, it is difficult to require concessions of developers. Generally, mechanisms such as density bonuses do not provide enough incentive for developers to participate in providing lower income housing.

2. Section 108 - How could the program be made more useful? Is more leveraging, targeting possible?

   Section 108 is one of the most effective and efficient programs in existence. We would recommend revising the regulations to allow greater opportunity for economic development activities, by increasing the maximum amount that can be borrowed and the term of the loan.

   The County of Los Angeles has utilized the Section 108 loan program to supplement various community development activities designed to eliminate blighted areas through land acquisition projects within the County and also within the participating cities. Just in the past two years $6.2 million in Section 108 loans has been generated for development projects that not only eliminated blight but upgraded the area through the increased tax base and the provision of job opportunities to the local community.

Our lump-sum drawdown accounts facilitate the following program benefits:

-- The public agency receives a 1/2 percent interest rate break on loans which creates a savings of up to $5,800 on every $100,000 worth of loans (based on a 12 percent rate loan versus a 12.5 percent rate loan). The overall expenditure in our Housing Rehabilitation Program is $3.5 million annually, thus a savings of $203,000.

-- The lender, as a result of the lump-sum deposit, designs programs utilizing flexible underwriting criteria of up to 50 percent debt-to-income (DTI) ratio for borrowers who would find it difficult to obtain loans through conventional lenders whose DTI ratio is normally 35 percent.

-- The public agency realizes an approximate 2 to 1 leveraging ratio of public to private funds as result of lender participation. For example, in funding $1,000,000 worth of 3 percent loans on an annual basis, the public agency saves approximately $550,000, which is the bank's contribution, as a result of the joint participation.

-- Programs are designed in cooperation with lenders to offer subsidized interest rate loans based on the affordability of the borrower. This is primarily accomplished as a result of the subsidies provided by the public agency which reduces the amount of possible risk and loss by the lender.

-- The borrowers receive more funds to repair their homes since the lender does not charge loan processing fees. If the public agency paid the fees, the cost per year would equate to approximately $36,000.

-- The Public Agency receives interest (passbook rate) on all deposits. The prohibition would reduce that program income, thus decreasing the overall effectiveness of the loan programs. The program income would normally be utilized in funding additional loans.

-- The lump-sum drawdown accounts provide incentives for lenders to continue to participate in the community and also provide direct benefits to low-income homeowners who wouldn't otherwise qualify for rehabilitation loans.

The County of Los Angeles opposes the proposed prohibition on "lump-sum drawdown."

The removal of the lump-sum drawdown feature would reduce the ability of rehabilitation specialists to design affordable loans programs that directly benefit low-income homeowners.

Throughout the years, the number of major lenders who participate in these types of programs have declined to one, namely, Security Pacific National Bank, through its Community Development Center. The elimination of this incentive feature would serve to exacerbate this cooperative relationship and make it more difficult for the CDC to address the needs of low-income homeowners and would add to the ever increasing deferred maintenance of our existing housing stock. This would occur at a time when funding from all sources is on the decrease.

3. What inappropriate impediments are in the way of economic development under present CDBG structure?

Every CDBG dollar invested in economic development activities has the potential of generating $10 dollars in private investments to provide projects that generate revenue and create jobs. The use of CDBG monies for economic development projects should be encouraged and impediments eliminated.

In the past several years, the County of Los Angeles made available approximately $35 million for economic development activities. However, we have had problems in getting private investors to take advantage of this opportunity. Developers are apprehensive about the numerous and complex requirements of "Necessary and Appropriate Determination," enforcement and monitoring of job creation and retention for low- and moderate-income persons.

Developers perceive the requirements as obstacles that outweigh the benefits. Further, the complexity of the requirements do not take into consideration the specific needs and capabilities of the small businessowner.

Most commercial rehabilitation loans are being provided for facade improvements. Although businesses would favor expansion rather than cosmetic renovation, economic development requirements are so stringent that private participation is discouraged.

I will cite an example of a project in which we were involved in La Puente which points up a separate but related problem concerned with the applicability of Davis-Bacon prevailing wage requirements when CDBG funds are used.

The City of La Puente invested $225,000 in a $4 million project which created 36 jobs and retained 8 jobs; 28 of these are occupied by low- and moderate-income persons. Through the City's CDBG participation, the project costs were inflated approximately 20 percent by triggering Davis-Bacon. (e.g. A painter in Los Angeles County normally receives $10 to $15 per hour. However, Davis Bacon prevailing wages require payment of $25.35 per hour to perform the same job.)

Relative to HUD business loan guidelines, these guidelines reflect the lending practices of the 60's - they should be reviewed and revised to make them more responsive to the needs of participants in order to achieve our national objectives.

4. What impediments have we found in CDBG housing development? What changes to the law would be beneficial?

With the exception of the inability to use CDBG funds in new housing construction, we have had significant success in effectively using CDBG monies for community development in the unincorporated area of the County and in our 51 participating cities.

Los Angeles County utilizes the HUD formula in allocating CDBG funds to its participating cities. Cities are allowed to locally determine how these funds should be used. We monitor the cities and the programs carefully...in fact, we operate as a mini-HUD in Los Angeles County, to ensure that all projects meet HUD regulations in every way.

Relative to the question about what refinements to the law we would propose, we strongly oppose any changes to the low/mod benefit ratio.

Although a substantial number of low/mod persons may reside within City boundaries, they are not necessarily concentrated in contiguous census tracts. In addition, the 1980 census data we are using to qualify a project is outdated and does not reflect the actual population and location of low- and moderate-income persons. Consequently, more of our projects are classified slum and blight because of the inability to qualify low- and moderate-income areas. For that reason, more direct benefit activities, such as housing rehabilitation and public services, are being provided.

The number of participating cities requesting a waiver of the 15 percent limit for public services has increased substantially. Therefore, an increase of 60 percent to 75 percent of the total allocation would further hinder program implementation.

Although Los Angeles County spends 80 percent on activities that benefit low- and moderate-income one of the most effective uses of CDBG funds is the ability to target money in marginal areas to arrest decline. Increase of the low/mod requirement eliminates the flexibility to invest CDBG funds in these areas, forcing localities to forego the opportunity of community stabilization through the prevention of further decay.

CDC Recommendation

The Commission recommends that grant recipients take credit not only for the CDBG funds invested in a project, but also for the additional public and private funds generated from the CDBG contribution.

For example: If $1 of CDBG generated $10 private dollars, then $11 are actually being provided to benefit low- and moderate-income communities.

The Commission opposes the proposal that grant recipients should only take credit for the portion of low- and moderate-income persons that benefit from CDBG activities.

5. How would the housing component of CDBG continue to operate after HOP is created?

The National Affordable Housing Act provides authorization for $3 billion to the Home Corporation, a new agency in HUD, which will provide funding to expand affordable housing through the use of Housing Opportunity Partnerships (HOPs) to states and local governments for use in partnerships with private industry and non-profits

The HOP concept proposes a broad range of uses not restricted by the existing CDBG regulations affecting housing. HOP funds will be made available to states and localities partly by formula and partly by incentive allocation.

A revolving housing trust fund would be established for each state or locality participating in the HOP. Funds could be used for homeownership, rehabilitation, construction, reconstruction, and also for relocation.

It is not yet clear exactly how the CDBG housing programs will coordinate and interface with the HOP programs. The manner in which allocation will be made to states and local governments needs to be clarified.

There must be some assurance that funding authorization for the Home Corporation will not diminish funding for the CDBG program. And further, since the legislation prohibits use of the money for administrative costs, this program must be incorporated into the existing CDBG structure of an organization without increasing administrative overhead. This is not realistic; reasonable administrative costs must be allowed.

6. Should a secondary market for CD loans be created? What would be the benefits and concerns?

Local Housing Finance Agencies and Community Development Divisions or Departments have long been in the business of making a variety of loans for housing or community development purposes. The loan documentation for these loans is highly individualistic and rarely bears any resemblance to other real estate documents in common usage in the real estate business.

Because of this lack of common standards, agencies often give away subsidies they are not aware of as in the case of unenforceable deferred loans that are really grants. Frequently there is no way to administer outstanding loans to assure that the public benefit is being accomplished. How many deferred loans have been assumed or wrapped in contracts of sale when investors purchase property from lower income homeowners?

The lack of standardized documentation makes it impossible for an agency to sell or transfer a portfolio of loans to another agency or even to transfer loans for centralized servicing.

The answer is for all of us to join together and to form a SECONDARY MARKET for the purpose of buying and selling community development loans; for buying or selling the servicing of community development loans and for establishing common documentation for the various types of loans. Expertise from the banking industry, from Fannie Mae or Freddie Mac, could be obtained. Escrow companies that currently service such loans could participate in developing the standard documents and contracts.

Local agencies, cities and non-profits would be the principal beneficiaries. Capital could be moved to the projects in which these entities are involved. Private foundations could make donations by participating in loans meeting the standards of the Secondary Market. State Housing Finance Agencies could sponsor tax-exempt general obligation bond issues to buy up community development loans from local communities, infusing new capital at the local level and contributing to the efficiency of loan administration.

The private sector has long understood the value of capital markets in moving funds to where they are most needed. It is time for the public sector to profit from their experience.